

**PROPERTY RIGHTS AND THE ROLE OF GOVERNMENT:**

**The Problem of Property in North Sea Oil.**

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## ABSTRACT OF THESIS

This thesis considers the implications of a combination of changes in property rights resulting from state intervention. It is argued that the resulting modifications in the exercise of property rights are a response to the limited adequacy of private ownership as a framework for economic activity, and that, in some cases at least, rights to state property may fulfil the same socio-economic functions as property rights for the private interests concerned.

In Part I, the case of property in North Sea oil provides for a detailed empirical study of this. The origins, evolution and extension of the UK system of petroleum licensing to offshore waters are considered. Particular attention is given to the retroactive amendment of licence terms through the Petroleum and Submarine Pipe-lines Act 1975, and the introduction of majority state participation through the agency of a state oil company, the BNOC. It is argued that, in spite of a considerable degree of state intervention, the licensing arrangements have assured the oil companies rights akin to property rights.

In Part II, conceptions of property are considered in the light of the foregoing study, especially those of MacPherson, Reich, and Pashukanis. It is concluded that a conception of property which emphasises its connection with convertibility helps explain the maintenance of private control in this case.

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## INTRODUCTION

### The Socialisation of Private Property

Capitalism as a mode of social and economic organisation is in decline. While all societies must reproduce themselves or cease to exist, capitalist societies are unusual in having reproduced themselves only at the price of partially destroying their capitalist character. So great has the change been that in the latter half of the twentieth century, it has become almost *de rigueur* to use the concept of capitalism only with a qualifying adjective or prefix like 'modern' or 'late' or 'neo-'.<sup>1</sup> Some, following Daniel Bell, have even rejected the concept altogether in favour of a new and often vague alternative concept like 'post-industrial' society.<sup>2</sup> In retrospect it is clear that one period of capitalist development, whether it be described as 'competitive' or 'classical', has given way to a new phase, characterised by large-scale state intervention in economic production and exchange, and a growing role for new states possessing the raw materials necessary for capital accumulation.

In this context it is hardly surprising that some writers like C.B. MacPherson and Charles Reich should have argued that it is now time to revise the individualist conception of property long associated with capitalism.<sup>3</sup> State intervention in particular seems

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1. For example, A. Shonfield, Modern Capitalism; Ernest Mandel, Late Capitalism, and Robin Blackburn, 'The New Capitalism', in Robin Blackburn (ed.), Ideology in Social Science, pp.164-186.
  2. Daniel Bell, The Coming of Post-Industrial Society. See Krishan Kumar, Prophecy and Progress, for a discussion of this trend in social theory.
  3. C.B. MacPherson (ed.), Property, and Charles Reich 'The New Property' in 73 Yale Law Journal (1964), pp.738-87, and in shortened form in MacPherson, op.cit., pp.177-198.



to have modified the role of the institution of private property in the advanced capitalist societies to such an extent that the dominant liberal conception has become problematic, if not redundant. My objective in this study will be to take their ideas as a starting point for a consideration of the impact of state intervention upon conceptions of property.

The above writers - I shall call them the New Property theorists - have argued that the liberal conception of property should be 'broadened' to include a number of rights not normally associated with it like the right to a social security payment. They claim that such a redefinition would be in line with current social changes which have blurred the distinctions between proprietary and non-proprietary rights. For example, legislative restrictions on the use and disposal of property in means of production have become quite common in the advanced capitalist societies.

While I believe their argument is mistaken, it does seem to me that we might benefit from considering the hypothesis that some non-proprietary rights can fulfil the same social and economic functions as rights of property. This need not compel us to revise the dominant conception of property as private property, but it may throw light on a paradoxical idea implicit or explicit in these and other writings on property and the state. The idea has two core propositions:

1. the institution of private property has been modified by the imposition of statutory restrictions upon the right to use and to alienate;

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2. at the same time some rights have been created which are tantamount to rights of property although not recognised as such by law (licence rights, for example).

This idea - that property rights in general have been 'restricted' relative to their nineteenth century predecessors at the very time that other rights have acquired a quasi-proprietary status - has a material basis in the real changes in property-ownership, occurring in recent decades. I attempt to explain what this social basis is and draw out some of its implications by reference to a theory of capitalism worked out by Marx and developed by Lenin. I also attempt to highlight and, briefly, to discuss some of the problems about property resulting from state intervention, in the light of my empirical research into petroleum licensing in the UK sector of the North Sea.

In recent years there has been a burgeoning of interest in property-ownership. There has been a new concern with justifications of private property,<sup>1</sup> with concepts of property,<sup>2</sup> with the institution of private property<sup>3</sup> and with the relationship between

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1. For example, Robert Nozick, Anarchy, State and Utopia; Lawrence G. Becker, Property Rights; Samuel L. Blumenfeld (ed.), Property in a Humane Economy; Derek L. Phillips, Equality, Justice and Rectification.
  2. For example, C.B. MacPherson, op.cit.; Carl Wellman (ed.) Equality and Freedom; Carol C. Gould, 'Contemporary Legal Conceptions of Property and their Implications for Democracy', a paper presented to the World Congress on Philosophy of Law and Social Philosophy, at Basel, Switzerland, August 27 - September 1, 1979.
  3. For example, John Scott, Corporations, Classes and Capitalism; Arthur Francis, 'Families, Firms and Finance Capital', in 14 Sociology (1980), pp.1-27; Paul Hirst, On Law and Ideology; Richard E. Flathman, The Practice of Rights. Some recent writing leans heavily on applications of new classical economics begun by Harold Demsetz: 'Toward a Theory of Property Rights', 57 American Economic Review Papers and Proceedings (1967), pp.347-359. Two recent examples are R. Posner's An Economic Analysis of Law, ch.3, and Kenneth Dam's study of petroleum leases and licences in Oil Resources.



legal and 'economic' ownership.<sup>1</sup> A striking feature of much of the writing is its North American origin. The notion of property has a much greater practical role to play in US constitutional doctrine than in the UK, and this seems to have provided American theorists with an impetus not yet shared in Britain. The New Property theories are very much a product of a non-British constitutional environment. The designation of particular rights as rights of property has a far greater practical significance in the USA where property rights are given special protection by the Constitution (5th and 14th Amendments) than in the United Kingdom where the doctrine of parliamentary sovereignty allows the State to exercise power over property rights as readily as over any other rights (cf. compulsory purchase). As a consequence, there must always be an element of juridical insecurity in relationships between private interests and the state in the UK.<sup>2</sup>

Yet this revival of interest has not come about as a result of pressure from the property owners themselves. Indeed, a feature of capitalist development in the twentieth century has been the surprising diffidence toward theories of property on the part of

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1. For example, Charles Bettelheim, Economic Calculation and Forms of Property; Nicos Poulantzas, Classes in Contemporary Capitalism; Piers Bierne and Robert Sharlet (eds.) Pashukanis, pp.235-272; and see Posner op.cit.
2. See the discussions in Geoffrey Marshall, Constitutional Theory, chs. 2 and 3. Throughout this study I have used the term 'state' without a capital letter, a usage common in the social sciences but not to purely legal writings. However, when the term has some specific legal reference, e.g. to international law in chapter two, section 1, I have preferred to write it with a capital letter.



the owners themselves in the face of state interventionism. This was remarked upon by several Marxist writers at the beginning of this century. Both the Austro-Marxists (like Hilferding, Renner)<sup>1</sup> and the Bolsheviks (like Lenin, Pashukanis) put forward the thesis that advanced capitalism or imperialism no longer has the same need for certain tenets of liberal thought in order to justify capitalism. This idea was based on several features of the social structure which either could not be found in laissez-faire capitalism or else had far less significance at that time. In at least two ways capitalism had become subject to a considerable degree of social control. Firstly, the concentration and centralisation of capital had progressed so far that large firms had an oligopolist role in the market. The resulting demand for large sums of credit from the banks gave an impetus to the concentration of banking capital: as a consequence the largest banks and firms had formed close links with each other in order to organise their business better. The size of the area in which these banks and firms (finance capital) could operate without hindrance had become a matter of the first importance. While finance capital operated transnationally, it remained based in one particular nation-state and existed in competition with the finance capital of every other advanced capitalist

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1. The Austro-Marxists represented a social-democratic appropriation of Marxian theory which had considerable influence in Central Europe prior to the First World War.

state. The second source of social control, state intervention, also had to be understood in the international context of oligopoly. A laissez-faire or 'nightwatchman' state had little relevance to the needs of such national capitalisms: on the contrary, finance capital required a strong state which could protect it from foreign competition and also use its political and military power to facilitate the export of capital. Intervention in the national domestic economy was welcome in so far as it assisted this phenomenon of internationalisation. Not only was there a change in the function of the state, but a limited socialisation of sectors of the economies of advanced capitalist societies was also tolerated by the ever-larger property-owners. It made little sense therefore to encourage elaborations or Revised Versions of the grand liberal theories which justified private property. Indeed, there was much support for Hilferding's thesis that the liberal ideology of the middle class was now in decline.<sup>1</sup> The ideas of trade, equality, peace and humanity were, he claimed, no longer suited to the reality of advanced capitalism, and were replaced by doctrines which sanctioned the expansion of finance capital: for example, nationalism, state power as a good (the *Machtstaat*), the worship of force (cf. Mosca, Pareto, etc.), and even racism. The relationship between contemporary liberalism and fascism was not so very distant.<sup>2</sup>

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1. Indeed, it has recently been appropriated by non-Marxists like Roberto Unger: Law in Modern Society, and Robert L. Heilbroner: Business Civilization in Decline.

2. This idea was developed philosophically by Herbert Marcuse in his Studies in Critical Philosophy.



The very property-owners themselves are no longer the individuals in the classical liberal theories: property-ownership has become de-personalised.<sup>1</sup> The individualist emphasis in all the various liberal conceptions of property has little correspondence to the contemporary capitalist environment. Socio-economic changes had struck so many blows against the single individual property owner even in the first quarter of the century that the disillusioned Schumpeter remarked:

The capitalist process pushes into the background all those institutions, the institutions of property and free contracting in particular, that expressed the needs and ways of the truly private economic activity.<sup>2</sup>

The market has been transformed from an arena in which many different companies, owned usually by individuals or family units, engaged in competition with each other to one in which a small number of very large corporations and financial institutions exert a predominant influence over it, attempting to minimise competition wherever possible. Traditional justifications of private property, whether the labour theory or the utilitarian, do not justify these particular concentrations of property as well as they do personal possessions. For example, the idea of accumulation taking place in Lockean fashion as a consequence of the individual mixing his labour with an object or soil to produce property for exchange presupposes a mode of production which is pre-capitalist.

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1. This is the dominant theme in the study by Scott, op.cit.
2. J. Schumpeter, Capitalism, Socialism and Democracy, pp.141-142.



In general, the liberal conception of property as private property, as a bundle of rights to exclude others from possession, use and management, and to benefit from any alienation of the object for profit, had a 'basic model' of ownership described by A.M.Honoré as one in which an individual human being (and his family) has control over an object or objects to use or dispose of as he wishes.<sup>1</sup> It is just this conception which lacks credibility in the face of advanced capitalism's oligopolic character.

Not surprisingly, there have been attempts to revise the liberal conception. With the exception of Robert Nozick who has re-asserted a highly individualist view of property, most liberal writers<sup>2</sup> have preferred to accept modifications to the classical view to allow for legislative restrictions to property-rights in the 'social' or 'national' interest. However, some writers like C.B. MacPherson and Carol Gould have gone further and have argued for a replacement of the liberal conception altogether.<sup>3</sup>

These various ways of re-defining property either within or outwith the liberal tradition are of course bound up with, and are a response to, real changes in capitalism in the twentieth century away from the individualism seen in its most extreme form in

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1. A.M. Honoré, 'Ownership', in Oxford Essays in Jurisprudence, First Series, (ed.) A.G. Guest, pp.107-147.

2. For example, Lawrence Becker op.cit., and Tony Honoré, 'Property, Title and Redistribution', in Wellman, op.cit., pp.107-116.

3. C.B. MacPherson, op.cit., and Carol Gould, op.cit.

nineteenth century Britain. Liberal writers, like Lawrence Becker, who accept a modified view of private property (particularly with respect to natural resources) are basing their re-definitions on the circumscribed character of property rights in contemporary capitalism. To do this they must make an assessment of certain 'social facts' like the expanded range of social and economic activities of the state. Some other writers in making such an assessment have drawn quite different conclusions about the impact of social change upon conceptions of property. Eugene Kamenka and Alice Tay, for example, have claimed that a complex of social and conceptual changes heralds a movement 'beyond bourgeois individualism' in the advanced capitalist societies.<sup>1</sup> Similarly, C.B. Macpherson points to the interventionist role of the state in the market to support his thesis that contemporary capitalism is a 'quasi-market society' and no longer needs the classical liberal conception which is only necessary to a full market society.

However, the critics of the private property concept have not themselves been free from criticism. Marxist writers have claimed that the reproduction of capitalist social relations has already required the partial relinquishment of key liberal ideas (like property) or at least a shift of emphasis to allow for a much greater degree of state regulation in the interest of capital units

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1. 'Beyond Bourgeois Individualism: The Contemporary Crisis in Law and Legal Ideology', in E.Kamenka and R.S.Neale (eds.), Feudalism, Capitalism and Beyond.



based in the nation-state (i.e. in the 'national' interest).<sup>1</sup>

In these new social conditions the liberal conception of property, stressing the inviolable character of property rights, is discarded whenever it might function as an obstacle to the accumulation of capital, giving rise to a more flexible view which tolerates ad hoc restrictions by the state, especially in wartime. Some writers go further and attack the liberal conceptions: for example, one American writer has asserted that:

The individual's right to life, freedom and property have no absolute or abstract existence; they are rights which exist, from the legal standpoint, only because the State protects them, and which are, as a result, entirely subject to the authority of the State.<sup>2</sup>

Yet there is sometimes an irony in this sort of criticism. The writer of the above passage, Harriman, and others who have held similar views, are in no way demanding an end to private property as such. Similarly, the once-fashionable attempts to refashion the liberal conception in some 'social' mould did not commit their advocates to a rejection of capitalist private property.<sup>3</sup> These lame attempts to conceptualise property in terms of an individual owner's 'social obligations' or in terms of

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1. On this latter point see Paul Mattick, Marx and Keynes.
2. E.A. Harriman, 'Enemy Property in America', cit. in E.B. Pashukanis, Law and Marxism, p.130.
3. For an account of these ideas, see Gottfried Dietze, In Defence of Property, pp.100-108. The reaction against individualistic conceptions of property originated in Germany in the late 19th century in the work of jurists and economists like Gierke, Ihering, and Adolf Wagner whose 'socio-legal' approach was scathingly criticised by Marx in his Marginal Notes on Wager. ✓



private property's social function were savagely criticised by E.B. Pashukanis.<sup>1</sup> In spite of using terms like the 'socialisation' of private property, these sociological jurists were not 'evolutionist' Marxists who, witnessing a growth of state property, saw in this evidence of the imminent demise of the private property system. These writers had by no means abandoned their commitment to the capitalist system,<sup>2</sup> and their re-definitions might even be construed as an attempt to justify a modified form of private ownership in advanced capitalism. Indeed, as Pashukanis noted, these 'social' conceptions of property had definite social roots in the new imperialist stage of capitalist development. It is this social context which encourages a form of anti-individualist social criticism. It is a form of criticism generated from within capitalism itself, and might be a useful, perhaps even essential, theoretical adjunct to the modifications in the institution of private property which are necessary to ensure the reproduction and expansion of private property as a whole.

Replacement of the dominant liberal conception of property as specifically private property is ultimately dependent upon replacement of the institution of private property as the dominant form of property in society with a different form of property. It is

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1. E.B.Pashukanis, Law and Marxism, esp. pp.34-35 and 98-99.

2. Ihering managed to combine his advocacy of a social orientation in legal thought with a publicly expressed admiration for Bismark and Kaiser Wilhelm the First. Private property and the right of inheritance would always remain, he thought, and 'the socialistic and communistic ideas directed to its removal I regard as vain folly' (Law as a Means to an End, p.396). Similarly, Duguit's idea of 'socialisation' ought not to be confused with Marx's. Ownership of the means of production would always remain in private hands, and private property predicated as usual: only the juridical concept on which its production was based would be changed. The proprietor, he claimed, had the duty and power both to use his property for the good of society, and for the satisfaction of his own needs. Thus he fulfils a social function, since any activity on his part benefits the social welfare.

not simply a matter of re-defining a nasty liberal conception which panders to the worst aspects of human nature, and, however reprehensible the reality presupposed by the conception is, it makes no sense to pretend that it is something else. What was most distasteful to Pashukanis about the 'social' conceptions was their ability to mislead people by their superficial radicalism and to conceal the individualistic character which property retained in the (relatively) new social environment. Nonetheless, it is a social environment which is far more organised and 'socialised' than ever nineteenth century capitalism was, and so questions about the continued relevance of the liberal conception are far from silly. While liberals prefer to remould the classical conception to fit the new social environment, others will see in contemporary capitalism agents of social control which point beyond the private property system, and thus provide empirical support for a new non-liberal conception of property.

In the early part of this century the principal socialising force which provided an impetus to revisions or re-assessments of property conceptions was the joint-stock company. The dismantling of much of the apparatus of state regulation after the First World War discouraged serious consideration of its role as an agent of social control until the extension of the public sphere was resumed after 1945. The Berle and Means thesis<sup>1</sup> that legal

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1. A.A. Berle and G.C. Means, The Modern Corporation and Private Property.



ownership was increasingly irrelevant to de facto control of large corporations led some to conclude that the traditional forms of private ownership in capitalism were disappearing and that the vast social power wielded by a small group of men through the large private corporations was influenced by considerations other than private gain: these were 'soulful' corporations, who had certainly made business deals but never with Mephistopheles!

The significance of the joint-stock company was the subject of protracted controversy between the 'theorists of industrial society' like Galbraith and Bell, and their critics (everybody else), but it did not generate much discussion among jurists and philosophers about the contemporary relevance of the liberal conception.<sup>1</sup> Of course, this debate has not exhausted itself, being renewed by the growth of multinational corporations and recently by the results of various impressive pieces of empirical research like that of Maurice Zeitlin,<sup>2</sup> which indicate inter alia that Berle and Means' thesis was premature. Nevertheless, systematic discussion of property and its legal structure tended to become the prerogative of sociologists, with jurists and academic lawyers confining themselves to brief comments, heavily influenced by the research of the former.<sup>3</sup> The

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1. Even in quite lengthy works on property like Reinold Noyes' The Institution of Property, and L.F. Vinding Kruse's The Right of Property.
  2. 'Corporate Ownership and Control', in 79 American Journal of Sociology (1974), pp.1073-1119; see also the study by Francis, op.cit., based on the Oxford Growth of Firms project.
  3. For example, Stein and Shand, Legal Values in Western Society; and Wolfgang Friedmann' Law in a Changing Society.

same reticence has not been evident in assessing the impact of the other principal agent of social control, state interventionism.

Large-scale state intervention began during the post-war period of social reconstruction and economic expansion, and has become a 'typical' feature of all advanced capitalist societies. As a consequence there has been a growth of interest in 'economic law' or the relationship between public law and economic policy.<sup>1</sup> So too has there been a growing interest in the relationship between the state and private property: what boundary lies between the public sphere and those vital private interests when the state can at will modify, amend, restrict or otherwise influence those interests? Is there a boundary at all? Writers like Lawrence Becker hope that by defining more precisely what property is and when restrictions on it in the social interest are justified, we shall have a clear picture of where the state may and may not tread. Other writers like Jürgen Habermas seem to think a 'politicisation' of capitalist society is inevitable.<sup>2</sup> Theorists like C.B. MacPherson and Charles Reich have based much of their New Property argument on the expanded role of the state: the interventionist role of the state in the post-war period (which I take to have ended with the onset

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1. With considerable problems of definition as a result, as Terence Daintith points out: 'Public Law and Economic Policy', in 9 ~~Journal of Business Law~~ (1974) pp.9-22.

2. Jürgen Habermas, Legitimation Crisis.



of global recession in 1973-4) created a situation, they claimed, which called for a new conception of property, broadening the application of 'property' to include at least some other legal relationships between individuals and the state like rights to receive welfare payments. While MacPherson locates his argument in a broader historical perspective to which property concepts are related, the new role of the state plays as important a part in it as it does in Reich's argument.

This latter view presupposed a model of capitalism suited to the socio-economic stability and uninterrupted growth of state intervention in the post-war period. However, the element of over-generalisation contained in its assessment of the consequences of state intervention is now apparent, and the New Property thesis has lost much of its plausibility. However apt its criticism of the dominant conception of property as private property, it nonetheless contains assumptions about law and the state which are firmly rooted in the liberal tradition. For example, they tend to view the state as primarily a neutral institution, giving little or no weight to those theories which see it as having a thoroughly partisan character. The extent to which the state can be, and has been, used to create new forms of property which co-exist and perhaps compete with private property is broadened as a consequence. Similarly, their view of legal language and legal structure exhibits a rather naive and uncritical acceptance of key liberal ideas like 'individual

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rights'. There is indeed a vast body of statutory regulation of individual rights to use and to alienate property, but, as sociologists and Marxists have been quick to point out, the legal structure of property relations is an important part of the institutional mediation of control but 'it is never the sole part'.<sup>1</sup> Indeed, Marx attacked the juridical conception of property because, like all key liberal ideas, it was market-based, and the market relations of capitalist societies failed to disclose the real origins of social inequality which were to be found in the relations of production, the presupposition of market relations. Besides, legal institutions like property have a considerable degree of flexibility which allows them, even when modified to accommodate an expanded role for the state, to have the same economic affect as in their earlier more absolute form. A final assumption which is both liberal and, in my view, wrong is that serious consideration of any major aspect of socio-economic life in the nation-state can take place without reference to the impact of international economic considerations upon that part of the social or economic structure. Since nation-states are not simply autonomous units, the interventionist activity of a state should be assessed alongside the internationally extending activities of the more efficient economic units based within its frontiers. There is an undisclosed national bias in the New Property thesis,

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1. Scott, op.cit., p.47.



a belief that we can comprehend the state at the national level or at the international level which may have corresponded to the reality of laissez-faire capitalism (although this too is contestable) but which is certainly not justified at a time when the international division of labour has become so complex and interwoven. We no longer have a choice.

In spite of these criticisms, which I elaborate in Part II of this study, the New Property thesis does point to a development of real significance. In order to stabilise the capitalist economy, the state has played a key role in regulating the use and disposal of property, but it has had an equally important role to play in providing the conditions which allow for an extension of capitalist relations and which may involve the creation of new forms of property-ownership. However, the origins of this 'new property' and its implications are very different from those contained in the arguments of the New Property theorists.

The paradigmatic type of property in capitalism is productive property and capitalist production is always production for exchange. Property for one's immediate use or personal possessions does not have the same social significance, nor is it the source of so many intellectual 'puzzles' as is property as exchange value. Consequently, it is quite mistaken to draw an analogy between certain 'citizens' rights' arising from the state's welfare functions and rights of property. The former category of

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right is not essential to the accumulation of capital, unlike property rights in the traditional sense (that is, as exclusive rights to use, management, income and to alienate). To apply the category of property to the former set of rights seems to me to be quite unjustified and thoroughly misleading. Nevertheless, a case might be made for an extension of the category to some rights deriving from legal relationships between individual corporations and the state which are necessary to the establishment of economic activity in relatively new conditions. After all, improvements in technology and changing economic costs may make certain economic activities possible and profitable for the first time: for example, the production of shale oil, and the construction of large-scale coal-to-oil liquification plants. However, such forms of economic activity might present problems for a system of full private ownership: the economic risks involved in large-scale production or the large initial investment may prove daunting even to the largest private firms; and the social risks of new technologies like nuclear power may create popular demands for state regulation. For these and similar reasons, relationships between the state and (usually large) private firms will tend to be established which involve the state in a highly regulatory and perhaps participatory manner. Arrangements involving the state in the latter capacity (like 'joint ventures') are at the present time much more common in underdeveloped countries than in the advanced capitalist societies but this has already begun to change, especially with respect to

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petroleum and mineral exploration and development. The rights which private interests have in these sorts of relationship may well be similar to property-rights (in productive property) in terms of their socio-economic function, even though there is a difference in legal form. This seems to me to be a line of inquiry worth pursuing not only because it may throw further light on the socio-economic significance of property in advanced capitalism, but also because of the light it may shed on the origins and the effects of legal agreements made between the state and large capital units in the advanced capitalist societies. Above all, it may reveal some ambiguities in the character of state intervention which the proponents of a new conception of property have neglected or ignored.

It is just such a line of inquiry which I intend to pursue in this study. In doing so, I shall draw on the theory of capitalist development found in the work of Marx and Engels and developed by various Marxists, especially Lenin. This was outlined briefly above and is explained in detail in the second part of the study. It has three salient features which I think should be emphasised at this stage. Firstly, state intervention is comprehended as merely one expression of a broad process of socialisation of production. Private companies have also introduced a degree of social control into their operations, becoming more concentrated in scale and international in their base of operations. Secondly, this theory strictly rejects any suggestion that nation-states can be viewed as autonomous units within an international context. On the contrary, it takes cognizance of the fact that the degree of interdependence has grown

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considerably in recent decades, and it claims that this means *inter alia* that an understanding of state action within its territorial boundaries cannot be obtained without an appreciation of its location in, and connections with, the capitalist world economy. Thirdly, socialisation will only occur when it can be accommodated within a capitalist framework. This is no simple matter: the process of socialisation is an attempt to resolve certain contradictions in the capitalist mode of production but it must not socialise the private relations of the capitalist economy out of existence. Since the objective is to ensure the reproduction and expansion of specifically private relations, that objective will function as a limit to any partial undercutting of capitalism's own premisses. Indeed, in so far as it is the capitalist mode of production which generates problems or crises requiring a non-capitalist solution, the reproduction of that mode of production will create the conditions for the reproduction of the same problems or crises whether capitalism has become partly socialised or not. The idea that the process of socialisation only has the effect of intensifying the basic contradictions in the long-term is an essential one in Marxism's understanding of this process.

These three features of the Marxist theory of capitalist development help to reveal crucial weaknesses in attempts to 'go beyond' the conception of property as private property, like those of the New Property theorists. At the same time they help explain why such theorists have no difficulty in finding social developments which seem to provide empirical support for their arguments.

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In spite of these criticisms of their arguments, I nonetheless intend to pursue their idea that state intervention can establish certain rights to property which have the same effect as rights of property, and should therefore be understood as property. However, instead of looking at rights to property created by the state's welfare roles (like the expectation of an income in the form of a welfare payment) as an example of 'new property' rights, a much better case can be made with respect to the state's control of natural resources. Rights to state property in natural resources can, and in some cases do, provide the same sort of benefit to capitalist firms as rights of property.

Property in natural resources is a key area of conflict in the advanced capitalist societies where private interests are frequently directly involved in their exploitation. In the last decade, there has been a growing tension between state and private control over their exploitation. Oil is the best example of this, being the most essential fuel in these societies, central to the post-war boom and still a low-cost fuel relative to alternatives. It is used as a raw material in the production of commodities like plastics, synthetic fibres and chemicals.

In my empirical study I direct attention to the licensing of North Sea oil because the rights of a petroleum licensee to oil resources seem to be an excellent example of 'new property'. In addition, they point to the highly ambiguous character of state intervention. The terms of a large number of licences were unilaterally revised without compensation by the Petroleum and Submarine Pipe-Lines Act in 1975, and licensees subsequently lost

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control of 51% of their production to the newly established state oil company, BNOC. In spite of this exercise in 'socialisation' of licence rights, the degree of economic control given to holders of licences issued before this time was not radically altered.

In the first part of this study I examine empirically the fundamental legal relationship between private companies and the British state with respect to offshore oil exploration and production: the licensing arrangements. The system of licensing is one which implies a high degree of state regulation through the model clauses included in each licence.<sup>1</sup> Indeed, licensing in its various forms is often seen as a mode of state 'control'.<sup>2</sup> In this case, however, the licences have a contractual character as well. Rights are granted to the licensee in model clause 2 in return for a commitment to invest capital resources in petroleum exploration. The regulatory and contractual elements in the licence co-exist. However, licensing arrangements were substantially modified by the Labour Government through the Petroleum and Submarine Pipe-Lines Act 1975 and further modified by the introduction of majority state participation in 1975-6. This alteration in the terms of licences already allocated to include a greater element of state regulation was presented as an exercise of social control over the large private firms involved. The idea that oil produced from North Sea

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1. I have in mind here only petroleum production licences for seaward areas, and it is such licences that I shall be concerned with throughout this study.
  2. See, for example, the discussion in Glanville L. Williams, 'Control by Licensing', in 20 Current Legal Problems (1967), pp.81-103.



fields was 'national property' provided the justificatory basis for the legislation.

However, I shall argue that this type of licensing is merely the principal legal aspect of a socialisation of economic activity which is a pre-requisite for the involvement of any private companies on a large scale. Ultimately, licence rights have an economic function analogous to that of property rights, although the difference in their legal character has the consequence of introducing an element of uncertainty into the relationship between licensees and state. Offshore oil exploration and the development of oilfields could not have taken place without a high degree of state regulation nor could it have occurred so rapidly without the involvement of large private companies on a contractual basis. Nonetheless, the solution of one set of problems creates another set of problems following from the relationship established between state and private parties. The high degree of state regulation and the possibility of unilateral alteration leads to considerable uncertainty about the stability of a licence arrangement. The state is obliged to wear two 'hats': firstly, it acts as political power, introducing an element of regulation into the market, assuring the private parties of their interests and interactions, and motivated not by considerations of profit but by the 'public interest'; and secondly, it presents itself as a party to a contractual arrangement, promising to act just like a private party. This twofold character of the state's presence is incorporated into UK licences: they possess a contractual character and at the same time they are the principal mode of state

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regulation. The limits of that state regulation are fixed by a particular constellation of political and economic interests which may be expected to change over time, as indeed may the priorities of any particular interest or interests involved.

The first chapter, 'Private Property and the State: the case of North Sea oil', is largely introductory. The principal conflicts contributing to a decline in private ownership and control are explained, and I provide something of a curriculum vitae of the international oil companies. The terms on which these companies are allowed access to oil from producing countries have changed: new forms of legal agreement place the companies in a contractual relationship with the state through the medium of its national oil company. In spite of losing title to the produced oil, the companies have so far retained control over its disposal. A similar development has taken place with respect to offshore oil development in the UK. However, it is essential to note the differences in the forms of state: an advanced capitalist state like Britain which is the home-base of two oil majors will have an entirely different relationship to the international oil companies than that of an industrialising state like Iran or a traditionalist state like Saudi Arabia. In section 3, I show how state regulation through oil licensing originated in the UK for reasons explicable mainly in terms of Britain's imperialist role in the world economy: its extensive overseas interests and economic rivalry with the United States.

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In the last section I show how the question of ownership of oil gains significance only when the oil is actually produced from the ground and becomes a commodity. The combination of state ownership of the oil in situ and the state regulation through the model clauses of licences can present a 'corporatist' picture of state involvement. This is rejected and I point to the 'nationalist' dimension as one way of explaining the British state's motivation for regulation of oil development.

In chapter two (Oil Companies and the State, 1962-74), I show how the licensing framework originated in an attempt to overcome obstacles to petroleum exploration created by the private property system or capitalist relations of production. The various companies conducting seismic surveys in the North Sea in 1962 were not willing to engage in proper drilling until the British state intervened to establish firm legal conditions. It did this by extending its sovereignty offshore, dividing the continental shelf area into blocks and establishing a system of licensing which allowed monopoly rights to be granted to private companies. These legal arrangements provided licensee companies with an assurance that their investment would be protected both against other states and against other private companies. The scale of investment required and the high risk involved rendered this security factor very important.

There was another factor which encouraged state intervention: economic rivalry between Britain and the United States. Given the preponderance of American companies in the international oil

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industry, the decision to depend upon private companies to explore and develop any resources on the continental shelf implied that American companies would do the lion's share of the work. A major reason for choosing a discretionary mode of licence allocation was that it would allow British Governments to discriminate against American applicants and in favour of British ones.

Throughout this period there was very little state regulation. Apart from encouraging the participation of private British companies, state intervention was mainly directed at securing the fastest exploration of the UKCS to benefit the balance of payments and provide a share of economic rent. While there was some state participation it neither assumed the form nor the scale which might lead to any conflict between the state's role as regulator and as participator. The licensee's economic control deriving from the licence gave him rights over any oil or gas found the character of property-rights.

The increase in oil prices and insecurity of oil supply during the oil crisis of 1973-4 persuaded the British Government to amend the terms on which oil companies extracted oil from the North Sea. The advent of a Labour Government with a manifesto commitment to increase 'state control' over oil development led to a conflict with holders of licences already allocated. In chapter three, I show how the Government strove to accommodate this commitment to the existing interests of licensees not only by making amendments to its legislative proposals but by issuing an invitation to the oil

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companies to discuss and suggest amendments to the proposals throughout the legislative process. The consequences of this are explained.

The Government was of course quite competent to ask Parliament to revise the terms of licences already allocated even though these licences had a contractual character. The doctrine of parliamentary sovereignty ensured that its course of action was in no way invalid. Nonetheless, a controversy developed about the character of licence rights: were they or were they not rights of property? This question was not satisfactorily resolved, although the material interests involved (payment of compensation, implications for British investments overseas) were made clear.

In chapter four I examine the other aspect of the Government's regulatory proposals: the establishment of a British National Oil Corporation (BNOC). This was a major new element in the legal regulation of oil exploration and development in the UK, but a common enough institution in all other oil-producing countries, except the USA. One major objective was to achieve 51% majority state participation via the BNOC in all commercial oilfields, and I show how this was done through a series of voluntary negotiations with holders of pre-1974 licences. By examining the legal agreements reached between licensees and the BNOC, it is clear that, in spite of the very different proprietary arrangements which resulted, the economic control over the oil held by the licensees was maintained: at least sufficient economic control for them to extract the resources as they see fit, sell it, and make the substantial profit

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which provided the motive for the initial investment.

By examining the constitution of the corporation we can see that the form of participation was not, initially at least, free from contradictions testifying to a tension between the regulatory and operating aspects. This was subsequently recognised and resolved by the Conservative Government in 1979.

In the second part I consider the question of 'new property' in a theoretical way, reflecting also on the results of the empirical study in the first part. While it is customary to begin a thesis with a statement of the problem and then a review of the extant literature, I have preferred to state the problem and to sketch my perspective in a preliminary way in this Introduction, and begin straight away with the empirical study. I hope in this way to attain maximum plausibility for the idea that a 'new property' can exist as well as to illustrate in a vivid manner the relevance of the perspective sketched out here, and developed in chapter five.

The work contained in the following four chapters is original in two senses. Firstly, the wide range of sources I have consulted are original ones for the most part: official reports, legislation (i.e. including Statutory Instruments), parliamentary debates of both Houses, interviews with some of the people concerned, reports produced by stockbroking firms, newspapers (The Financial Times, The Times, The Guardian, and The Scotsman) and specialised journals. I have also consulted books like the 'UK Oil and Gas Law

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Manual' of Professor Daintith and G.D.M. Willoughby and have attended one conference and two seminars on this topic organised by the Law Society and the International Bar Association. Obviously, some sources were more important in some chapters than in others. For example, interview material is used almost exclusively in chapters three and four. Of particular assistance for chapter one, were the 'Materials' for the Honours course in Oil and Gas Law at the University of Dundee.

Incidentally, the study does not presuppose any familiarity on the reader's part with the technical terms peculiar to the oil industry. I have taken as much care as I could to explain the meanings of particular technical terms as and when they appear in the text.

It is also original in the sense that nothing has yet been written which utilises the mass of empirical material relating to oil licensing in the UK North Sea in a social scientific way, as distinct from accounts of 'the law' or 'histories' of law and policy since 1964. Although my own perspective is an historical one, it is not an account of 'events'. Neither does it claim to be comprehensive in its treatment of oil company-government relations in Britain during this period. Fiscal legislation, for example, is not considered, on the ground that it does not present the same problems of property and the state's dual role as licensing does. I do not of course deny its important role in securing a share of the rent for the state.

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**PART I:**

**The Conflict over Property in North Sea Oil**



CHAPTER ONE

Private Property and the State:

the case of North Sea oil.

With an ever greater share of wealth-producing activities occurring at sea, policy decisions are being taken by governments which will affect profoundly the allocation of world resources and the relationship between the public and private sectors. It is widely assumed that institutions such as the price system and private property which have been cornerstones of the economic system in Western developed countries, can play only a minor role in offshore developments.<sup>1</sup>

Kenneth Dam

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1. K.W. Dam, 'Oil and Gas Licensing in the North Sea', in 8 Journal of Law and Economics (1965), p.51.



Contents:

1. Conflicts in the production of oil
  - (i) producers v. consumers
  - (ii) producers and consumers v. the oil companies
  - (iii) private property v. oil
2. The international oil companies
3. Oil and the British State
4. Ownership of North Sea Oil

## 1. Conflicts in the Production of Oil:

In the twentieth century oil has assumed the role of the most important fuel for industrialised societies, whether capitalist or communist, taking the role which coal had for capitalist societies in the nineteenth century. However, there are several sources of conflict in the production of oil which contribute to a decline in private ownership and control of this resource. These conflicts are: (1) between producing and consuming states; (2) between private companies and both kinds of State; and (3) between the private property system and the particular geological conditions in which oil is found. I shall say a few words about each of these sources of conflict in turn.

### (1) Producers v. Consumers

A principal feature of the world oil economy is the geographical separation between the major markets for oil consumption and the location of major oil deposits. The principal consuming states are the highly industrialised capitalist economies of the United States, the United Kingdom, France, West Germany and Japan. However, the major oilfields are located in the Middle East, in West and North Africa, in Central and South America, and in South East Asia. As a consequence, much crude oil is transported in pipelines and tankers. More than one half of the cargoes transported by sea are made up

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of oil. Professor Chevalier claims that 'each day more than 80 million tons of crude (or half the production of Kuwait's oilfields) are at sea'.<sup>1</sup> Until recently the chief supply routes converged on the two main importing areas: Western Europe and Japan. However, the USA is rapidly becoming a third major importing area as its domestic supplies diminish.

The Soviet Union is also a major consumer of oil but it is at the same time a major producer, and thus stands apart from the main traffic in the world oil economy. Oil exploitation was begun in Russia in the late nineteenth century by European companies searching for oil supplies as an alternative to the near monopoly which Rockefeller's Standard Oil had achieved over American oil products. After the nationalisation of 1917 production was increased to obtain self-sufficiency in oil. At the present time it is the world's major oil producer. In 1979 its oil output was running at an average of 11.7m barrels a day; more than 2m barrels a day above Saudi Arabia's current production.<sup>2</sup> Since its oil is consumed almost entirely within the Soviet bloc I shall not dwell on this topic further.

Until the late 1960s the relations between producer and consumer states were organised largely by the actions of the seven largest private oil companies known as the 'Seven Sisters'.

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1. J.M. Chevalier, The New Oil Stakes, p.8.

2. The figures comes from The Financial Times, November 23, 1979: 'The enigmatic giant'. The USSR is also the world's leading producer of metallic minerals and coal.

Their role will be discussed separately in section two of this chapter. However, the last decade has seen a growth of control by the oil producing countries, organised in O.P.E.C., over many aspects of oil production: pricing, control over production rates, etc.

From the late 1960s onward, these states acted to increase their control over oil found within their national boundaries. They have not all moved at the same pace nor attributed the same significance to the same modes of control. However, despite individual differences they have managed to act collectively through OPEC with considerable success.

There were three ways in which the 'OPEC Revolution' took place. It involved:

1. Seizure of control over pricing by OPEC and the assertion of the right to set prices unilaterally.
2. Seizure of control over production levels; in other words, the ability to reduce output if the particular states wished to.
3. Seizure of control over the physical oil distribution system. This had two stages:

(i) OPEC countries nationalised the oil production facilities and replaced oil company control with a framework of medium-term lifting agreements, mostly with the majors,<sup>1</sup> and then

(ii) these were replaced after 1978-9 with more detailed and restrictive contracts, with a wider range of would-be

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1. The interests of BP, Shell and the Compagnie Francaises des Petroles (CFP) in Iraq were nationalised in December 1975. At the same time, negotiations between the Kuwaiti Government and the two oil majors, BP and Gulf, were taking place with a view to nationalising the companies' outstanding 40% share in producing operations.



purchasers (for example, the supply contracts between the Iranian Government and Japanese oil companies, signed in January this year<sup>1</sup>). The ability of the oil majors to adjust supply in order to meet fluctuations in demand was thus undermined.

This was by no means a unilinear development: OPEC was formed in 1960, and made little progress in realising any of the above goals until the early 1970s.<sup>2</sup> Taking advantage of a combination of factors (principally high demand combined with a world shortage of tankers), it forced a dramatic increase in oil prices in 1973-4, and the Arab members imposed a production cut-back in October 1973. The price increase was, however, followed by a sharp fall in real terms between 1974 and 1979. It was only the Iranian Revolution in 1979 which re-created the right market conditions for OPEC to take advantage of and to initiate another sharp rise in the price of oil.

The demands of the producing states for higher prices and for greater control over the development of their resource have arisen not merely from their perceptions of its ruthless exploitation by foreign oil companies over the decades. In their view the major consumers have benefited greatly from plentiful supplies of cheap oil and should now pay its real worth. In addition, the distance between some consuming states like the UK and the USA and 'their' oil companies is not considered great: to put it bluntly, they are frequently seen as one arm of US or UK foreign policy. Hence

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1. See 'Iran signs new oil supply deals' in The Financial Times, January 4, 1980.
  2. There are various accounts of OPEC's history but that of Stork (Middle East Oil and the Energy Crisis) has the merit of stressing its conservative character: see especially chapter 8. A recent and sober assessment of OPEC can be found in International Affairs, vol.55 (1979) pp.18-32: 'OPEC's importance in the World Oil Industry' by Edith Penrose.

the OPEC actions are levelled at the consuming states as well as, if not more than, the oil companies.

The response of consuming states has not been uniform, but in general the mood has been one of alarm over OPEC's new role. Oil has a strategic character for the advanced capitalist economies in both the military and the economic senses. Indeed, the International Institute for Strategic Studies has stated the most serious security challenge for these societies in the 1980s in the following terms:

How to ensure the supply, from an unstable Third World, of the raw materials on which its economic well-being, domestic stability and political cohesion have come to depend.<sup>1</sup>

The consumer states have acted in at least two ways to deal with the problem of insecurity of supply. Firstly, they have acted individually and collectively, through the International Energy Agency, to reduce their dependence upon external supplies of oil. However, this has not led to any significant reduction in dependence upon mainly Middle Eastern sources of supply. Secondly, they have attempted to find and/or increase indigenous sources of supply of oil or oil-substitutes. This has been stimulated by the price rises which have made some sources 'economic' for the first time: for example, 'marginal' oilfields in the North Sea. To achieve this, a considerable increase in state intervention has been necessary: private firms working in the energy sector have been reminded of their social obligations in this way.

One must, however, be cautious about the increasing state intervention in the consuming states: it does not necessarily imply

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1. Cited in 'Threat to West's raw materials' in The Financial Times, May 16, 1979.



a decline in the role of private companies in the production of oil within their national boundaries. Some writers<sup>1</sup> have neglected the fact that the forms of state involved are quite different from those in the producing countries. The establishment of a state oil company and a petroleum revenue tax does not make the British State resemble the State of Saudi Arabia except in the most superficial sense. This point requires some elaboration.

In the last decade there has been a trend toward increasing control by producing states over their oil operations. With the exception of the United States, this has been a universal phenomenon. Despite the fact that it is the home-base of two of the major oil companies, Britain has followed this trend since 1974 by establishing a national oil company and introducing 51% majority state participation into all commercial oil fields in its offshore waters. It also introduced a special petroleum tax and increased its body of regulatory controls.

One interpretation of this trend, and particularly of state participation in Britain, is that it indicates a 'decline' in the role played by the private oil companies. The growth of social control, in the form of state ownership and direct participation, is obtained at the expense of private enterprise. For example, J.C. Woodliffe asserts:

The last decade has witnessed on a global scale a dramatic shift in the balance of economic and political power between

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1. To name but a few: T. Daintith and I. Gault, 'Pacta Sunt Servanda and the Licensing and Taxation of North Sea Oil Production' in 8 Cambrian Law Review (1977), pp.38-9; 'The general tenor of the developments in domestic policy here described is a familiar one in the context of oil company-Government relations the world over.' (at p.38); J.C. Woodliffe, 'State Participation in the Development of United Kingdom Offshore Petroleum Resources', in Public Law (1977), at p.249; K. Chapman, North Sea Oil and Gas, p.98; Kenneth W. Dam, Oil Resources: Who gets What How?, pp.3-20.

the multinational oil company and the sovereign nation state, whether it be a producer or consumer of oil. Nowhere is this change<sup>1</sup> in relationship more evident than in the United Kingdom.

The present position, he claims, shows a movement in the direction of greater state involvement.<sup>2</sup> Such a view neglects the different forms of state involved, as well as exaggerating the consequences of certain legal changes. It is particularly inappropriate as a view of the development of state intervention in the UK.

Indeed, the distinction between producer and consumer states can be criticised for the same reasons. It abstracts from one feature of their national economies (whether they are net importers or exporters of oil) and ignores their different degrees of industrialisation and their different political structures. It also neglects their role in the world economy.

I have merely used it in these introductory pages to sketch a general and preliminary picture of the world oil economy and the tensions within it. It has been quite sufficient for my purposes to consider as consumer states only the principal consuming countries like the USA and the UK.<sup>3</sup> These are also advanced capitalist societies and their states are imperialist<sup>4</sup> in character. The fact that both the USA and the UK are substantial producers of oil should not obscure this imperialist aspect, deriving as it does from their economy and state taken as a whole. By focussing solely upon oil

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1. 'State Participation', op.cit., p.249.
2. loc.cit.
3. There are of course many other 'consuming countries' in the so-called 'Third World', like India.
4. See chapter five for an explanation of what I mean by 'imperialism'.



policies and the municipal petroleum law it is of course possible to find similarities in the actions of all producing states in the last decade. Nonetheless, the real determinants of a state's law and policy on petroleum development are to be found in its socio-economic structure and in the dynamic of the world economy. In Britain's case, the salient feature in this context is the complex network of economic links between the largest British firms and banks on the one hand, and the industrialised and industrialising nations on the other.

(ii) Producers and consumers v. the oil companies

Until the late 1960s oil companies operating in many parts of the world had been able to secure for themselves the ownership of oil produced by their operations in return for a payment of royalties and other taxes. One advantage of this was the ability to conduct a profitable business in selling surplus 'owned' crude oil to other companies.

However, a climate of economic nationalism in the producing states led to the nationalisation of company assets in a number of states. The nationalist mood was conveyed in a remark (made somewhat earlier) by Sheikh Abdullah Tariki:

We are the sons of the Indians who sold Manhattan Island.  
We want to change the deal.<sup>1</sup>

The nationalisations began in Algeria in 1971 and in Iraq in 1972, taking place at a time when agreements between OPEC and the

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1. Cited in J.E. Hartshorn, Oil Companies and Governments, at p.312.

oil companies about increased control and revenue for the producers were reached and subsequently revised in Tehran, Tripoli, Geneva and in New York. In 1975, Kuwait negotiated the acquisition of the remaining assets of Gulf and BP, while Iraq simply seized the remaining assets of foreign oil companies. Negotiations followed in Qatar and Saudi Arabia which resulted in takeovers of company assets.

The international oil companies were still to have a role. They were to be employed as contractors on an ad hoc basis working for fixed fees. In most states, however, the bulk of the state's oil production is now sold back under contract to the former concessionaires. The major part of the oil which does not go back to former concessionaires is sold under long-term contracts. These are highly flexible arrangements, containing three-month re-opener clauses so that the terms applying to either volume or price may be adjusted: this makes them 'contracts of long intention' rather than long-term contracts.<sup>1</sup>

The form of legal agreement between producing state and oil company (or companies) reflects the change in economic power and has been characterised on the analogy of Maine's famous dictum as a movement from concession to contract.<sup>2</sup> The old concession has been described by Northcutt Ely as

...essentially a contractual agreement between a company and

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1. For an elaboration of this, see 'Oil Companies adapt to a new role', in The Banker, March, 1977, p.85.
  2. 'From Concessions to Contracts': two articles in The Petroleum Economist, December 1974, pp.459-61; January 1975, pp.21-25.



a government which confers certain rights and corresponding obligations upon both parties. It is also a document of title against which money can be borrowed.<sup>1</sup>

The element of title has now been removed and the present arrangement is a contractual one of the kind described above. The very idea of a 'concession' has been discredited, since it carries overtones of colonialism. Its purpose was simply to hold one social and economic relationship in a country stable for usually very long periods of time. Paradoxically, success in the fulfilment of this task eventually led to accelerated change.

The decline in the role of the oil companies can be seen not only from the success of these nationalisations but also when these measures are seen against the background of earlier attempts at nationalisation of foreign oil companies' assets. These had occurred in Russia in 1917, in Mexico in 1938, and in Iran in 1951. In the first case it was part of a revolution and preceded a civil war in which the Tsarist forces were partly funded by the oil companies whose interests had been expropriated. In the second case, a virtual boycott of Mexican oil by the major oil companies followed nationalisation, and led to such a slowing down in exploration and production that further substantial quantities of oil were not recovered for 30 years.<sup>2</sup> Finally, there is the case of Iran. After the industry was nationalised in 1951, all production

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1. Ely, 'Changing Concepts of the World's Mineral Development Laws' in World Energy Laws, IBA, pp.47-69.

2. The dispossessed companies threatened legal action against anyone purchasing oil from the new Mexican state oil company, thus preventing exports until the Mexican Government agreed to pay compensation: the same strategy as that adopted by Anglo-Iranian during the Iran crisis in 1951.

ceased and the Anglo-Iranian Oil Company (now BP) threatened to take legal action against any entity which bought and used 'its' oil. Since the Iranian oil industry lacked the legal right to sell abroad the oil produced from concessions which had been granted in accordance with customary international law, no Iranian oil was sold on world markets. A settlement was only reached after the CIA staged a coup and restored the Shah to power in August 1953. The Shah took as his adviser on petroleum affairs Thorkild Rieber, a former chairman of Texaco until he was forced to resign in 1940 for alleged pro-Nazi sympathies.<sup>1</sup>

The privately owned oil industry has therefore become more subject to the control of the producing states. However, this phenomenon has extended even to the consuming states. For the most part, these states have shown little reluctance in increasing state regulation over the basic sectors of their economies like steel, coal, gas and electricity: this extends to oil too.

The post-war expansion of the international oil companies in Western Europe led to various forms of state intervention in many countries, even before the oil crisis of 1973. Oil was placed partly in the public sector by the establishment of a state oil company in France, Italy, Norway, Austria and Finland. Governments also attempted to influence company decisions on refining and pricing in their 'national interests'.

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1. J. Stork, op.cit., p.54. Kermit Roosevelt, the CIA man in charge of the coup later left 'public service' to become vice-president of Gulf Oil. The State Department and the CIA were controlled by the Dulles brothers: John Foster Dulles previously worked for the law firm of Sullivan and Cromwell, which represented the Rockefeller oil interests; Allen Dulles had an association with American interests in the Middle East going back to World War I.



The United Kingdom proved something of an exception to this. Before 1975 there was a conspicuous lack of state regulation, despite the existence of a burgeoning domestic oil economy. An attempt to introduce a state oil company in the late 1960s failed (see next chapter). This situation changed dramatically in 1975 with the creation of a state oil company, and legislation of new licence and taxation arrangements.

The United States was another very different case. Few large corporations arouse as much hostility in the USA as the large oil companies. As recently as 1976 a Bill was introduced in the Senate to divest these companies of much of their assets.<sup>1</sup> Pressures upon the oil companies came from the ecology lobby, and from advocates of a free market who resent the oligopolist role played by the companies and threaten to use the anti-trust legislation to reduce that role.

However, in both the latter cases, any conflict between the state and the oil companies (national or internationally operating) is qualified by an awareness of common interest. The international oil companies are either American or British based<sup>2</sup> and make massive contributions to their countries' balance of payments.<sup>3</sup> The British Petroleum Company is the biggest exporting company in the United Kingdom. Further, these companies have

... effectively organized their activities around the world behind the guarantee of security offered by the political

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1. For an account of this, see The Times, February 23, 1976: 'Senate Bill to break up oil groups'.
  2. Shell has its operating headquarters in London.
  3. For example, the UK balance of payments benefited by £1,100 million from BP's North Sea activities in 1978 (BP Annual Report, p.7).

and/or military presences of the United States and the United Kingdom.<sup>1</sup>

(iii) Private property v. oil

The third source of conflict over property found in the production of oil derives from the peculiar natural characteristics of oil. The exploitation of some natural resources, and oil in particular, has presented difficulties for systems of private property. One legal authority has observed ironically that

... the search for an answer to questions on property-rights in petroleum has been, scarcely less arduous than the search for petroleum itself.<sup>2</sup>

Oil is like coal and other minerals in being a finite, non-renewable resource, but it differs from 'hard' minerals in possessing a fugacious character. It is found in structural traps in reservoir rock below the surface, and accumulates in the pore spaces of a variety of sedimentary rocks, like sandstone and limestone. Extracting it, according to one writer, is 'more like squeezing treacle out of a brick than lifting bucketfuls from a well'.<sup>3</sup> The oil is capable of migrating through the reservoir in which it is found to areas of low pressure created by the drilling of wells. It will do so with no regard for the boundary lines of surface owners.

If a reservoir should extend under land which has several different owners, as is common in the USA, one of the owners could

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1. P. Odell, Oil and World Power, p.190.

2. G.D.M. Willoughby, 'Property Rights in Petroleum', in The Law Society's Gazette, January 11, 1978, p.6.

3. Gerald Foley, The Energy Question, p.132. A good account of these geological features is contained in A.F. Fox, The World of Oil, pp.57-9.



not exercise his rights to the resource without disadvantageously affecting the rights of others. It follows from the oil's fugacious character that oil cannot be extracted unilaterally if a reservoir reaches under the area of several owners or licensees. As oil is taken out of the ground, the remainder will prove more difficult to extract, requiring expensive recovery techniques and will therefore be worth less.

The consequences of this for a system of private property were first encountered in the USA.<sup>1</sup> Originally, the dominant rule was the accession rule: the right of property in subterranean mineral deposits rests in the proprietor of the surface (*cuius est solum, eius est usque ad coelum et ad infernos*). However, this was modified at an early stage in one of two principal ways. Firstly, it was assumed that analogies could be made between oil and wild game or percolating water (in fact oil cannot percolate through subsoil over great distances). From the analogies US judges constructed a 'rule of capture' which had the effect of modifying the accession rule. This 'rule of capture' simply meant that the oil belonged to whoever could get it, and the surface owner's right to the deposit was made subject to it. As a consequence, he would lose title if oil under his land were drawn off by drilling on adjoining or nearby property. Alternatively, the surface owner was denied the ability to exercise full rights of ownership over such a volatile commodity at any point prior to reduction to possession at the wellhead.

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1. For an excellent account of this, see Chevalier, *op.cit.*, pp.45-7; see also T.C. Daintith, 'The UK Petroleum Regime', in Proceedings of the Petroleum Law Education Trust Seminar, held at Cambridge, January, 1978 (hereinafter Proceedings), IBA, vol.I, paper 4.

The result of these modifications of the accession rule was drastic for the production of oil. There was a destructive proliferation of wells as rights to produce were sold off in small lots and each owner tried to produce as much as possible from his piece of land. A multiplicity of private owners and lessees drilled wells and extracted oil at a feverish pace in competition with each other. This had two immediate consequences: firstly, a surplus of oil was created, leading to a lowering of prices; and secondly, considerable wastage of oil resulted from the competitive drilling and extraction. State intervention followed and a system of 'pro-rationing' established whereby each field was to be treated as a whole and rights to the oil in situ were apportioned among a number of different lessees or owners. Drilling and extraction was carried on at a controlled rate and waste prevented.

Although this phenomenon has only been seen in the United States, full private ownership and the rule of capture has become a 'bogey' which legislators in other States have struggled to avoid.<sup>1</sup>

As early as 1917 the British Government was persuaded by S. Pearson and Son to introduce a scheme of state licensing of oil exploration.<sup>2</sup> Apparently, the assumption was that at common law, the rule of capture or something very similar would be applied by courts in the UK to modify surface owner's rights, with the attendant

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1. In fact there are several systems of ownership in the USA: title to minerals and hydrocarbons may exist in the Federal government, the state government, or an individual, depending on surface ownership.

2. For a fuller discussion of this see section 3 below.



risk of competitive drilling. Before the Pearson company would act as an agent to explore for oil deposits this matter had to be clarified. I shall return to this in section 3.

The expansion of oil exploration and production into offshore waters on the continental shelves of States has added to existing problems about property in oil. In the United Kingdom it is not absolutely clear what the exact character of rights possessed by the Crown really is ('sovereign rights'). Similarly, there is some doubt about the character of the rights possessed by licensees in the oil and gas in situ under the Continental Shelf, since the international regime seems to exclude the ownership in fee system adopted for onshore deposits by the Petroleum (Production) Act 1934. In addition, it is not clear whether the ownership in fee principle is qualified by a rule of capture.<sup>1</sup>

However, there is a clear trend toward state regulation as a means of combating the adverse effects of unfettered competition among private owners and licensees. As the state itself has come to assume ownership of all petroleum deposits in situ, the basic legal relationship between private owner, lessee, and the State has been replaced by one between the State and an operator, usually holding a licence as opposed to a lease or concession. It is now also the norm for a State to function as a partner in the operations,

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1. These problems are discussed in a general way by T.C. Daintith in 'World Energy Laws: Surveys and Prospects', in World Energy Laws: Proceedings of IBA Seminar on World Energy Laws held in Stavanger, Norway, May 1975. Some clarity may be emerging with the passage of time: see the discussion in Terence Daintith's paper, Correlative Rights in Oil Reservoirs on the United Kingdom Continental Shelf, paper presented at the European Offshore Petroleum Conference and Exhibition in London, October 24-27, 1978.

through the medium of a state oil company.

This has not brought an end to problems about property, particularly in the new offshore areas of exploration and development. To the extent that private oil companies are employed by a State to exploit oil resources, the fugacious character of the oil will compel different licensees sharing the same reservoir to reach agreement as to how and when it is to be exploited and in what proportions the oil is to be divided.

Before I examine these matters, some words must be said about the various private owners of the means by which oil is produced and distributed.

## 2. The international oil companies

Large private firms in the advanced capitalist societies certainly dominate these economies but they can no longer function within the national framework: they must, as Paul Mattick notes, 'become and must remain multinational corporations'.<sup>1</sup> Another author notes:

Any company of importance that wants to survive has to be international and multinational, (since) companies with worldwide operations may find it easier than purely national companies to reduce costs by moving raw materials, production and distribution facilities, and manpower in conformance with optimization objectives.<sup>2</sup>

The petroleum companies were the pioneer international corporations. Of all capitalist enterprises they were the first to adopt a worldwide strategy of profit maximisation, the first to locate a

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1. Marx and Keynes, p.262.

2. G.A. Steiner, cit. in Mattick, op.cit. p.262.



large amount of their assets outside their home countries, and the first to depend on foreign-derived income for more than half their profits. There are no better examples of the use of oligopoly power than the ways in which these international oil companies controlled markets, fixed prices and reduced competition over a period of several decades.

The following table, showing the rank and turnover of the world's largest industrial companies in 1978, shows the prominent place which the largest oil companies have in the world capitalism:<sup>1</sup>

1.	General Motors	63.2 \$ billion
2.	Exxon	60.3
*3.	Royal Dutch/Shell	44.0
4.	Ford	42.8
5.	Mobil	34.7
*6.	BP	27.4
7.	Texaco	26.8
8.	Standard Oil (California)	23.2

The asterisked companies are British or partly British based; the others are all American.

In fact not all the oil companies are the same size. We can divide the companies into three groups: firstly, the majors; secondly, the independents, and finally, the national oil companies.

The majors, or the 'Seven Sisters' as Enrico Mattei called them,<sup>2</sup> are the largest of the internationally operating oil companies. They are Esso, Shell, BP, Mobil, Chevron, Texaco and Gulf.<sup>3</sup>

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1. Source: The Economist, December 29, 1979; 'The Giants'.

2. Enrico Mattei was the head of Ente Nazionale Idrocarburi (ENI), the Italian state oil company until his death in a mysterious plane crash. Under his direction, ENI tried to obtain alternative sources of oil to those controlled by the majors.

3. Esso is the trade name of the Exxon Corporation, otherwise known as Standard Oil of New Jersey.



These companies are responsible for about 80 per cent of all the oil production in the world outside the United States and the <sup>communist</sup> socialist States. They also own or control over 70 per cent of the total refining capacity in these areas, and operate directly or indirectly through long-term charter fifty per cent of the tonnage of internationally operating tankers.

Since they control most of the refinery capacity and market outlets in Western Europe, these companies are the biggest buyers of oil. Their bargaining strength is considerable, since as Kenneth Dam points out they have

... a wide range of ventures in progress, of which operations within any one country's jurisdiction will normally constitute only a minor proportion. Many are well-capitalised companies with the capacity to generate internally cash needed ...<sup>1</sup>

The fact that their operations are international does not however imply companies owned and/or controlled by several nations. It only means that their operations are world-wide, employing citizens of many different countries and having nationally registered subsidiaries in many different states. Their leading personnel, their shareholders and their basis of operations are <sup>almost entirely</sup> limited to those of three nations: the USA, Britain, and Holland.<sup>2</sup>

In general, these companies or 'groups' consist of a top holding company with numerous associated and subsidiary operating companies. Each is integrated vertically, controlling most of its own requirements of crude oil, owning or controlling through long-term charters most of its own transport facilities, owning its own

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1. Oil Resources, p.32.
2. The Dutch involvement through Shell is of minimal significance relative to the other two nations.



refineries, and controlling its distribution outlets all over the world. The separate 'groups' are often closely associated through joint ownership of subsidiaries and through long-term supply or marketing agreements (e.g. the Arabian American Oil Company, Shell-Mex BP). They are also in competition with each other, this taking the form of attempts to maintain or increase their shares in the markets for final products or to obtain a position in new markets, through strategic acquisition of raw material supplies and refinery and distribution facilities, through improvements in products and through advertising. Price competition (pre-1973) was always avoided as far as possible and market-sharing agreements were not unusual. Selling crude oil has not been their main interest since most of their profit until recent years came from the production of crude oil.<sup>1</sup>

The national character of these companies is often given too little weight. In some accounts, like Anthony Sampson's,<sup>2</sup> an almost rigid separation between the 'economic' and the 'political' is presupposed: their autonomy from their home state is treated as almost absolute. The erroneous character of this view is best illustrated by looking at the relationship between the USA, the home state of five of the 'Seven Sisters', and the

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see Turner + also  
Church Report  
pp. 2-3.  
(notes)

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1. E. Penrose, 'Middle East Oil: the international distribution of profits and income taxes', in The Growth of Firms, Middle East Oil and Other Essays, pp. 140-1.
  2. The Seven Sisters: the Great Oil Companies and the World They Made.

American based oil companies. However, this is well documented in most of the general studies of the oil industry and there is no need to repeat the details.<sup>1</sup> It suffices to note that this does not always take the form of direct assistance to the American majors in their foreign operations. A more complex form of support developed in the 1970s when the majors as well as the domestic oil industry and American business as a whole stood to benefit from an increase in oil prices: both sections of the American oil industry, domestic and international, would benefit from higher prices in terms of increased profits, while removal of the cost advantage given to their European and Japanese rivals by cheaper oil would benefit many American companies in the chemicals and textiles industries.<sup>2</sup>

American influence upon the international oil companies extends to the non-American majors, Shell and BP. Both companies have considerable assets in the US, and depend on their US subsidiaries for large proportions of their total income. The former is part-British and part-Dutch in ownership, but nonetheless insists that its non-American employees, if they are candidates for senior managerial positions, have periods of service in the US subsidiary, the Shell Oil Company, which is 60% owned by Shell International. According to Peter Odell,

... all the managing directors have been sent to work in the USA at various parts of their careers.<sup>3</sup>

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1. For a detailed account see Engler, The Brotherhood of Oil, pp.98-145, or Stork, op.cit. + Turner (best account)

2. This form of support is central to the explanations of the oil crisis of 1973-4 advanced both by Chevalier, op.cit. and Odell, op.cit.

3. Oil and World Power, p.21.



The US subsidiary is so large that it contributes about one-third of all the Shell Group revenues and profits.<sup>1</sup>

BP's involvement in the United States is even greater: nearly one-half of its current assets are located there. This is largely the consequence of its attempt to diversify its sources of supply away from the Middle East. In 1969, the Alaskan leases of BP's American subsidiary, BP Inc., were proved to contain 54% of the biggest oilfield in the Western World, the Proudhoe Bay complex. Since US legislation required the oil to be sold domestically, and since BP had no refining or marketing facilities, it sold most of its Alaskan interests to Sohio (Standard Oil of Ohio), a small domestic oil company possessing infrastructure but lacking access to crude oil. In return it obtained a stake in Sohio which was linked to oil production from Proudhoe Bay: as production increased, so did BP's share in the company. By 1978, BP had acquired majority control of a company employing 22,000 people and selling 20m tonnes of crude oil in the USA every year and had invested \$6.2 billion in Alaska. In addition, the two companies own nearly one-half of Alyeska, the trans-Alaskan pipeline operating company.<sup>2</sup> The strategic significance of this investment by a foreign company in the USA is considerable: the Proudhoe Bay oilfields contain over one-quarter of the proven crude oil reserves in the USA and BP, via Sohio, controls over one half of those fields. The possibility

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1. loc cit.

2. All the figures are from The Guardian, July 11, 1978: 'BP's Alaskan adventure pays off in the US'.

of political action against these interests was, as we shall see, one which vexed successive British Governments from the late '60s onward and influenced the pattern of UK oil policy.

By contrast, the concentrated character of these large firms is often given too much weight. Together the seven major oil companies dominate the international oil industry (and have eight large counterparts which dominate the huge American market). Their operations extend throughout all the stages in supplying petroleum products: until recently, ownership of reserves, recovery of crude oil, pipeline transport, refining and selling through service stations.

These few oil companies have always done most of the business involved in all phases of the industry. As early as the eve of the First World War, the seven majors already dominated the international oil market. One of them, Shell, was present at all phases of the cycle of production and possessed a highly diversified supply system. Two of them alone controlled the Middle East: the Anglo-Persian Oil Company and Shell.<sup>1</sup>

The term 'seven sisters' was coined by Enrico Mattei, the chairman of ENI,<sup>2</sup> to connote the degree of co-operation that existed among the majors. Both internationally and in the USA the largest oil companies have adopted a 'live and let live' convention, minimising competition among themselves and avoiding price-cutting. The opportunity to exchange thoughts on common policy has been facilitated by the fact that they frequently engage in joint operations.

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1. For a good account of the period up to 1970, see Chevalier, *op.cit.* chapter 1, pp.15-33.

2. See page 17, note 1.



The history of the oil industry provides famous examples of agreements to curtail competition: the Red Line Agreement made in October 1927 divided up the oilfields in the Arabian Peninsula among the majors and was not dissolved until 1948; the 'As Is' Agreement, made at Achnacarry Castle, Inverness-shire in 1928 supplemented this by ensuring co-operation in marketing as well as in production: they agreed to freeze the market at it was. However, this co-operation was only won by necessity, that is, the desire to conserve profits, and the agreements were broken whenever one of the parties thought it would gain an advantage by doing so. At the present time, it is not necessary for them to form a cartel since any rise in costs (or fall in profit) automatically leads to a rise in prices.

The reasons for this concentration can be found in the industry's history. It has been a history of shortage, fear of shortage and glut in turn and the hectic rising and falling of prices. Put simply, the industry is subject to over-supply, leading to the possibility of price collapse. Cartels have developed in order to keep prices up: those oil companies who were best able to diversify their risk did this.

There are a number of phases in oil production: exploration and production; transportation; refining; transportation of the refined product to the consumer; and marketing. Control of the various phases allows for an averaging out of respective profits in various phases, and so they have tended to be organised by the

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same corporate groups. Hence their concentrated character has been very evident to the general public. This horizontal integration (forward and reverse) helps to avoid problems of supply: shortage or excess.

Paul Frankel identifies two other features of oil production which have acted as a stimulus to concentration of private capital.<sup>1</sup> Firstly, the high risk involved in oil production: a well may be drilled at a site thought to be favourable from a geological point of view, but there is no way of being certain that a deposit will be found or that sufficient oil will be found to recover the expenditure on exploration. Technological innovations have reduced this problem, but have not eliminated it. Secondly, a high degree of fixed capital is required in oil production. The best example of this is the cost of constructing and installing production platforms in the North Sea.<sup>2</sup>

Both of these features encourage operating companies to minimise the risks involved, and one way of doing this is to diversify sources of supply. To do this successfully, a company must be of a certain size and hence there is a tendency toward concentration.

However, in spite of all this, the oil industry is not the most concentrated of industries. There is no single firm like IBM which dominates the entire industry. The biggest companies in the aluminium and the car industries have a much bigger share

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1. Paul M. Frankel, 'Structural Analysis of the International Oil Industry up to the immediate post-World War II Situation', in Proceedings (1978) op.cit., vol.I, paper 1.

2. A steel platform cost £155.2 million in 1975 (source: Department of Energy, North Sea costs escalation study).



of the market than the large oil companies have. All the major industries in advanced capitalism show a high degree of concentration and, whatever its peculiar circumstances as an industry, the oil industry is by no means exceptional in being highly concentrated.

The second group of companies are known as the independents. However, the term 'independent' is a rather misleading one: it is used to describe private companies which are smaller than the majors, although still large by comparison with most corporations and still privately owned. Unlike the majors they are often not integrated in their operations, being less secure in either sources of supply or outlets for their products and confined in their operations to a few countries or even one.

These companies are marginal operators and do not provide an alternative to the very large units. Paul Frankel describes them as the 'collapsible extension of the main structure'.<sup>1</sup> Competition between them and the majors certainly exists but has often been exaggerated. The involvement of independent companies exploring new areas like North Africa in the 1960s certainly influenced the majors,<sup>2</sup> and as early as 1962 and 1963 twelve independents were carrying out seismic surveys in the North Sea.<sup>3</sup>

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1. Proceedings, op.cit. at p.1.7.

2. See Chapter Two, p. 93.

3. First Report from the Public Accounts Committee, North Sea Oil and Gas (1972-3) H.C.122 (hereinafter PAC Report), p.83. These included Sun Oil, Phillips, Marathon and Envoy Oil. Five of the majors were also present.

Most of these companies are American owned, although some British independents like Tricentrol and Burmah secured interests in the North Sea and have received favourable treatment in licensing rounds organised under Conservative Governments. Many of these companies are organised in Brindex, the Association of British Independent Oil Exploration Companies.

The American independents first became a force internationally in the 1950s. They diversified their interests abroad to obtain cheaper supplies of crude oil than had been available from their fields in the USA and thus increase the profitability of their domestic refining and marketing operations. However, in response to the demands of domestic oil producers for a ceiling on imports of cheap oil, the Eisenhower Administration established an import quota system in 1959:<sup>1</sup> a mere 13% of US oil consumption could then come from abroad. Those companies which had made commitments to find, and produce and export oil were suddenly left without a market, and a general surplus of oil was created. The companies affected, like Occidental, Atlantic Richfield and offshoots of the Rockefeller Trust like Standard Oil of Indiana (Amoco), then proceeded to challenge the Seven Sisters' agreements of price control by offering crude oil to independent refiners at prices lower than the majors'. They also built their own refineries and made a variety of oil products available on the markets. The result was intense competition between these oil companies and the majors for the European and Japanese markets.

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1. See Odell, op.cit., pp.34-42, for an account of this.



This situation has ceased to exist since the 'OPEC Revolution'. In the face of the rising cost of oil, the independents have attempted to consolidate the modest share of these markets which they obtained.

The third group of companies are the national oil companies. It is more accurate, however, to call them state oil companies, since, as we have seen, the majors are also national oil companies of a sort. I shall, however, retain the conventional use in this study.

Just as all nations are not alike, so their national oil companies differ. Those companies established by OPEC states like the National Iranian Oil Company (NIOC) are an attempt to increase those countries' shares of revenue from oil development, and also to control rates of production. In addition, they have a symbolic aspect, representing an assertion of national independence against colonialism. However, national oil companies have also been established in the advanced capitalist states. In such cases, it should not be interpreted as a radical or socialist phenomenon: it is not an attempt to seize a commanding height of the economy. In the postwar period it proved popular among West European nations, like France and Italy, as a response to their lack of indigenous oil supplies and consequent dependence upon supplies from the Middle East, which was of course controlled by American and British companies.

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As a result of the growing fears of interruption to oil supplies which followed the oil crisis of 1973-4, national oil companies have assumed a greater importance in the advanced capitalist states. While attempts to introduce such a company had failed in Britain in the mid 1960s, a British National Oil Corporation was finally established in 1975, supplementing the state share in BP.

The reasons for the creation of national oil companies are not to be found principally in the realm of profit-making economic activity. There is rarely any claim that a national oil company will do anything better or more cheaply than a private oil company, and it may well be required to do things from time to time which will not be advantageous in this sense of the word 'economic'. Such companies are however now the norm in all oil-producing areas, except in the USA and in Chile.

The role of the privately owned oil companies in world oil production has changed dramatically since 1970. The price-fixing cartel of the Seven Sisters has been replaced by that of OPEC. As described in section 1, a wave of nationalisations reduced their dominance in the Middle East and North Africa. The methods by which they are granted rights of exploration and production have altered radically,<sup>1</sup> and they have lost the decision-making role over production rates in the most prolific areas which are controlled by the OPEC cartel.

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1. See 'From Concessions to Contracts', op.cit. For a history of the oil concession as a legal instrument in the Middle East, see J.E. Hartshorn, op.cit. pp.312-19.



The form of legal agreement itself has come to have 'overriding importance in view of sensitive political and nationalistic feelings'.<sup>1</sup> The trend has been away from the concession form which gave companies exclusive long-term rights over most of a country's territory in return for royalties and income taxes,<sup>2</sup> toward a contractual relationship based on methods such as joint ventures, participation arrangements or service contracts, with the state as owner. The notion of a property-right vesting in a foreign oil company, with corresponding rights of control, the 'theoretical cornerstone of the concession concept',<sup>3</sup> smacked of colonialism, of national rights being exchanged for 'baksheesh', and was therefore removed.

The significance of this development for the oil companies is hard to gauge. If a government has the power to unilaterally alter whatever arrangement is in force, it makes little difference whether it is a concession or a participation arrangement. Certainly the old concession terms were more favourable than the modern agreements: these give companies rights of property which are diminished by joint venture and participation agreements and eliminated by production-sharing contracts. However, even the concessionary rights could be effectively defeated by the host government if it chose to enact increased tax rates upon company operations.

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1. op.cit. p.459.

2. The famous D'Arcy concession, granted by the Persian Government to William Knox D'Arcy, gave him the exclusive right to explore for and exploit the petroleum resources of Persia, excluding five northern provinces, for a period of 60 years, and exemption from all Persian taxes. See Odell, p.29.

3. Ely, op.cit., p.43.

In all the various types of arrangement, the company or consortium contracts with the producing government to provide the capital and expertise required to develop the petroleum resources in return for a right to a share of the production.

The implications are stated quite bluntly by Northcutt Ely:

When all is said and done, what is important (to the companies) is how much oil the company is allowed to take away from its operations and at what cost. Whether its right to this oil is characterised as a "contract right" or a "property right" is less important, as a practical matter, than the amount of profits that the right produces. These profits do not depend on the nature or the type of agreement as much as they depend upon the specific terms of that agreement.<sup>1</sup>

The changes in the oil companies' role resulting from these new legal arrangements and from the dominance of the OPEC cartel over pricing and production ought not to be exaggerated.<sup>2</sup> The oil companies themselves have not remained passive in the face of a changing and less favourable climate in the main producing centres. Perception of a decline in profitability (or 'increasing cost'<sup>3</sup>) was already leading many companies, both majors and independents, to diversify their operations. This diversification has been of three kinds:

1. Diversification into competing energy sources like coal.

This was begun in the 1960s in anticipation of lower future profits in the Middle East, and has included all the major alternatives:

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1. op.cit., p.41. See also Tugendhat and Hamilton, Oil: The Biggest Business, at p.335: the problem is not one of the particular form of the concession but 'the security of tenure and precise financial terms attached to it'.
  2. For a sceptical view of the changes in the Middle East resulting from the new legal arrangements between governments and companies, see Dam, op.cit. pp.12-20.
  3. For the oil companies' point of view, the decline in profits is perceived as an increase in cost.



coal, gas, nuclear energy and hydroelectricity, and some of the minor ones like wind, wave and solar power. Coal has proved especially attractive since, like oil, it is a fossil fuel and requires essentially the same geological techniques to extract. Most companies, including BP since the 1970s, have extensive coal interests in the western states of America, Canada and Western Australia.<sup>1</sup>

2. Diversification into new sources of oil supply. This process also began in the 1960s when oil companies spent large sums of money looking for oil on- and offshore in Indonesia, West Africa, Alaska and the North Sea: in spite of a situation characterised by increasing supplies and weakening prices! In 1969, the American periodical 'Business Week' described this as:

... the wildest, and the most widespread oil rush in history ... in the face of an oversupply of crude so massive that if not one additional barrel of oil were found the world could maintain its current consumption for more than 30 years.<sup>2</sup>

The more recently discovered resources of oil have been found on public lands like Alaska. In the United States where one-third of all land and most of the undersea continental shelf is owned by the federal government, this has led to a conflict between oil companies and environmentalists.

Despite mixed success (not all areas are like the North Sea), the profits from Alaskan and North Sea oilfields have been so great

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1. 'Big Oil is buying rocks', in The Economist, September 16, 1978.
2. Cit. in Stork, op.cit., p.146. See also T.C. Daintith and I. Gault, op.cit., where the greater political and legal security of the North Sea is emphasised.

that they have provided the capital for a number of large takeovers by oil companies, and for further diversification.<sup>1</sup>

3. Diversification into economic activities unrelated to energy. This is also a process which began in the 1960s. Many oil companies have extensive interests in mining, where there is a technology overlap with oil extraction. Companies like Pennzoil and Kerr-McGee have diversified into extraction of phosphate and copper, as well as coal and uranium. In recent years, Atlantic Richfield has purchased the second largest copper company in the US. Several companies have diversified into more exotic areas like retailing (Mobil), office equipment (Exxon), publishing (Atlantic Richfield), and even farming (Kerr-McGee established itself in agricultural fertiliser production).<sup>2</sup>

In addition to this strategy of diversification, the oil companies have attempted to move the locus of profit from the producing to the consuming end. Consequently, their loss of ownership of reserves at the point of production need not imply a simple decline in their overall role. They still have considerable control over transportation, refining and marketing: in other words, over disposal of the oil. They can therefore manipulate the various markets for crude oil and finished products, distributing them only at the highest rates. Furthermore, the large price increases in 1973-4 and 1979 have increased company profits

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1. See 'Spreading, and clipping the oil majors' wings', in The Financial Times, September 12, 1978.

2. 'Big Oil is buying rocks', op.cit.



considerably: for example, in 1979 their profits increased by between 25 and 100%.<sup>1</sup> The rate of increase in official prices has been greater than the rate of increase in real costs, and price increases greater than the increases in company costs have been passed on to the consumers temporarily solving the crisis of profitability.<sup>2</sup>

In this section I have provided an outline of the international oil industry and have suggested that private control over the means of production and distribution has not been significantly diminished by changes in the legal arrangements between companies and the governments of producing countries. Most investment and organisation of production is still carried on privately.

Unlike those who emphasise the scale and multinational character of these companies, I have preferred to stress their national character. Indeed, not only are they nationally based but they are based almost exclusively in two advanced capitalist nations: the USA and the UK, with the former playing the dominant role. The relationship between the oil companies and their home-states is a close one as will be seen in the next section which deals with the case of Britain.

### 3. Oil and the British State

Long before the formation of OPEC, state intervention in the exploration and development of petroleum deposits had occurred in the UK. The idea that oil is a natural resource which 'belongs'

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1. 'US oil majors continue strong advance in profits', in The Financial Times, January 26, 1980; BP's after-tax profits rose by nearly four times in 1979 ('BP's after-tax profits soar to £1.6bn.' in The Financial Times March 14, 1980).
  2. The maximisation of profit is the sole objective of these corporations. Considerations of planning, for example, have 'no more replaced maximum profit than the jet aircraft has replaced motion' (M.A. Adelman, The World Petroleum Market, p.2).

to the nation has been a common one for decades. Indeed, the law established in 1934 to regulate onshore development through a licensing system also provided the legal basis for offshore development at a much later date (in 1964).

This early form of state intervention was obscured by the comparative lack of success of onshore drilling and also by the very conspicuous involvement of the British state in the international oil industry through Shell and BP. Yet the origins and development of the licensing framework provide an essential perspective upon the measures of 'socialisation' taken by the Labour Government between 1974 and 1976 (which I examine in Chapters Two, Three and Four).

There are in fact two forms of state intervention here. Firstly, there is state intervention in oil production indirectly through its majority shareholding in BP; and secondly, state intervention in the assumption of ownership of petroleum deposits onshore and, with qualifications, offshore as well. In this section I shall look at both of these in turn, with a view to ascertaining the consequences of the state's role for private production of oil. I do not consider for the moment the role of the BNO.

While interest in the possibility of indigenous sources of oil only arose during the First World War, the British Government had acquired a controlling interest in the Anglo-Persian Oil Company slightly earlier in 1907. The impetus to this action came from anxieties about 'national security'. Paul Frankel notes that:

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... even at the highest level of imperial and world power of the British, except for comparatively small quantities in Trinidad, there was no oil in the British Empire and Commonwealth on a large scale.<sup>1</sup>

This made Britain dependent upon oil supplies from the United States for the Royal Navy's oil-burning fleet. However, that dependence was minimised by the acquisition of a substantial shareholding in the Anglo-Persian Oil Company. At that time Anglo-Persian held the first of the Middle East concessions, the D'Arcy concession, in what is now Iran. Security of supply was assured since the Middle East was mainly a British sphere of influence from the beginning of the twentieth century onward.

The arrangement concluded between the original owners of the Company and the British Government provided the company with the capital it required to expand its oil operations, and, in return, allowed the Government to nominate directors of the company with a power of veto over the Board's decisions. The idea was that this would allow Government control over company policy and the disposition of produced oil.

The real situation was, however, rather different. Since that time, every Government has striven to assure BP, as it is now called, its independence in 'commercial' operations. In a discussion of its accountability in the House of Commons in 1965, the Prime Minister made some revealing remarks about this.<sup>2</sup> The Government-appointed directors have, he said, a general obligation to report on all matters which they consider should be referred to, or brought to

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1. Proceedings, op.cit., at p.1.5.

2. 711 H.C. (Oral Answer) (May 4, 1965), cols.1111-1113.

the notice of, the Government. These reports were made to the Treasury quite frequently but were 'mainly of an oral character': written official reports were not sent in. In the main they would not interfere with decisions which represented 'genuine commercial considerations'. The Chairman of BP has claimed that the company's decisions are taken

... commercially and without influence from Ministers ... (though) we probably have an advantage over anyone else in the closeness of our collaboration with government departments.<sup>1</sup>

There is considerable irony in this last remark in the light of the Bingham Report.<sup>2</sup> It seems that both BP and Shell had consultations with the Government in 1968 and 1969 which led them to believe that the Government would support their sending oil to the illegal Smith regime in Rhodesia. For several years these companies sent supplies of oil to Rhodesia via a circuitous route through Mozambique and thus undermined the effect of United Nations' sanctions. Whether or not successive Governments knew of this (and some members certainly did) is less important than the support given to the companies by the Government in 1979 by refusing to prosecute the companies concerned.<sup>3</sup>

Successive British Governments have indeed provided considerable support for BP in its international operations, especially in the company's attempt to secure sources of oil outside the Middle East in

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1. First Report from the Select Committee on Nationalised Industries, Nationalised Industries and the Exploitation of North Sea Oil and Gas (1974-5) H.C. 345 (hereinafter NISC Report), Minutes of Evidence, Q.576, 581.
  2. Report on the supply of petroleum and petroleum products to Rhodesia, by T.H. Bingham and S.M. Gray, 1978. See also Martin Bailey, Oilgate.
  3. See remarks by the Attorney-General: 976 H.C. (December 19, 1979) cols. 627-39.



the face of nationalisation threats. The two main thrusts of this effort were: firstly, a huge investment in the North Sea, and secondly, the exploitation of Alaskan oil through the gradual transfer of Standard Oil of Ohio to BP.

With regard to the first, the Conservative Government intervened as early as 1962 to suggest that Shell undertake joint exploration work in the North Sea with BP. Shell then proceeded to make overtures to BP, which resulted in one of the North Sea's strongest partnerships.<sup>1</sup> BP's stake in offshore operations in the North Sea is very large, amounting to 9% of the licensed territory in 1977.<sup>2</sup> Similarly BP was given diplomatic assistance in its efforts to establish itself in Alaska and the United States. By the early 1980s, BP's access to American and North Sea crude oil will be slightly larger than Exxon's.<sup>3</sup>

However, the company has never been used as an instrument of policy. The right of veto held by the Government-appointed directors on the Board has not in fact been exercised, and the nearest a Government actually went toward 'controlling' the company occurred in October 1973 when the Prime Minister, Edward Heath, tried to compel BP (and Shell) not to reduce their oil supplies to Britain. The chairman, Sir Eric Drake, was reminded that the Government had a controlling share in the Company but would still

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1. See NISC Report, Appendix 18.
2. Woodliffe, op.cit., p.255. It has proved lucrative too: according to Lord Kearton, chairman of BNOG, it made a profit to £1 billion on the Forties Field by Spring 1979 ('Small is beautiful to the Tories - or is it?' in The Observer, May 13, 1979).
3. The Economist, June 18, 1977: 'High-octane salesmanship for BP's super-blend'.

not accede to the request unless he was told which other countries would suffer as a result and the request was made in writing.<sup>1</sup> At this point Mr. Heath backed down.

The major obstacle to use of BP as an instrument of Government policy has always been the extensive overseas operations of the company. Shortly after the oil crisis the idea was once again discussed with respect to the Government's proposed changes in North Sea operations but was rejected because 90 per cent of the company's operations were overseas.<sup>2</sup> It was thought that 'the use of BP would bring serious repercussions in relation to other oil companies', and two areas in particular would experience 'problems': Alaska and BP's retail outlets in the USA.<sup>3</sup>

The de facto relationship between BP and Government is then rather different from the one which may be inferred from the de iure one. Nor is the de facto relationship absolutely stable. Opposition to BP's 'relative autonomy' was very evident in the autumn of 1978 when the Labour Party National Executive Committee issued a policy statement demanding that BP and its subsidiaries be nationalised. This demand followed publication of the Bingham Report and was supported by the then Energy Secretary, Tony Benn, also a member of the Committee. At roughly the same time, the Department of Energy also made known its dissatisfaction with the Government's relationship with BP. Apparently, BP failed to consult the Department over several major decisions, including

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1. The incident is recounted in Anthony Sampson, *op.cit.*, p.263.
  2. NISC Report, para.75.
  3. *loc.cit.*



purchase of assets worth £43m. in Western Europe. One of the Department's objectives seems to have been to require BP to report directly to it and not to the Treasury as has been the custom since 1914.<sup>1</sup>

In spite of this, the de facto relationship between Government and BP shows no sign of changing. Indeed, BP's 'autonomy' has been reinforced by two recent developments. Firstly, the Government shareholding has been substantially reduced. From 1914 until 1967 it had held the majority of the share capital but in that year it fell to 48.2%. Following the collapse of Burmah Oil Company Limited in 1974 it increased, as Burmah's 21.5% shareholding in BP was transferred to the Bank of England. In an attempt to raise money for public expenditure a sale of BP shares was held by the Labour Government in 1977. Nicknamed the 'sale of the century' it represented an unprecedented sale of public assets, equivalent to one-fiftieth of all the shares held by all the investing institutions in the UK.<sup>2</sup> The government was left with a share of 51% once the Burmah shares were included. Another, smaller, sale held by the Conservative Government in 1979, reduced this further. Secondly, the Government authorised the Bank of England at the time of the 1977 sale to assure potential applicants for the shares that it would

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1. 'State may change its link with BP', in The Financial Times, October 18, 1978.
  2. 'The drama behind the huge BP share deal' in The Financial Times, June 18, 1977. US investors received a 20% allocation of the shares on offer, and 'every City house of standing' was involved, thanks to the Bank of England: see account in The Guardian, July 1, 1977: 'Anger in US at BP shares bungle'.

not alter its relationship with the company. The offer document stated that:

It is the Government's intention to maintain its relationship with BP in a way which does not breach the traditional practice of non-intervention in the administration of the company as a commercial concern.<sup>1</sup>

It is often forgotten that state intervention in oil exploration and production took place on a considerable scale with respect to onshore oil deposits. This occurred in two phases: in the period 1917-18 and in 1934, and was designed to facilitate private exploration and production by providing a legal framework which removed certain barriers to the operations of private companies.

The origins of petroleum licensing in Britain lie in war. During the First World War, the Government, anxious to find secure sources of fuel supply, introduced a Bill to encourage the exploration and development of possible onshore petroleum deposits.<sup>2</sup> The provisions dealing with the establishment of a royalties fund to remunerate existing owners under whose land exploitable oil deposits might be found proved unacceptable to Parliament, and the Bill was dropped. Instead, the Government made a new regulation under the Defence of the Realm Act 1914 authorising its agents to enter privately owned land to search for

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1. Cit. in The Financial Times, October 19, 1978: 'BP and the Government'.

2. This and the following paras. owe much to the account of onshore licensing law up until 1964 contained in Terence Daintith and G.D.M. Willoughby, A Manual of United Kingdom Oil and Gas Law (hereinafter Manual), pp.10-13.



and extract oil deposits, and to prevent others from doing so.

There was still considerable confusion about the law on property in petroleum deposits at this time: the Government was uncertain as to whether or not a rule of capture existed at common law, and hence the possibility of unrestricted competitive drilling.<sup>1</sup> This matter was raised in an exchange between the Government and S. Pearson and Sons, a British company with extensive oil interests and operating experience in the USA and Mexico. The company offered its services to the Government but emphasised the need to avoid the unrestricted competitive drilling which had led to a great waste of resources (and fall in profits) in the USA. A condition of the company's offer to act as agent was that a permanent legislative framework be enacted by the Government, which would prevent competitive drilling.<sup>2</sup>

The outcome of this exchange was the Petroleum (Production) Act 1918. This Act left the contentious issue of property rights in petroleum in situ alone, and tackled the problem of competitive drilling by forbidding any searching or drilling for oil except by persons holding a licence granted by the Minister of Munitions or persons acting on behalf of the Government (like Pearson's). The prohibition applied to surface owners as well as to others, but they retained the right, by denying entry to their land, to prevent even licensees from operating. Apparently,

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1. The Government seems to have assumed that, in 1917, United Kingdom courts would have applied the rule of capture to modify surface owners' rights. This is doubted by Professor Daintith (Proceedings, op.cit., at p.4.2).
  2. Letter scheduled to Agreement Between Minister of Munitions and S. Pearson and Sons Ltd. Cmd. 9188 (1918); extracts are contained in Materials for the Oil and Gas Law Honours course at the University of Dundee at C.102.

this Act 'was viewed strictly as an interim measure to get Pearson's operations under way'.<sup>1</sup> In the event, the results of Pearson's drilling proved too poor to merit intensive drilling and the company soon gave up. Very few attempts were made to explore for oil under licences granted under the 1918 Act.

Nonetheless interest in onshore petroleum deposits revived more than a decade later. This time private companies were more concerned about the need to negotiate with a multitude of surface owners than about the possible threat of competitive drilling. In 1934, the National Government<sup>en</sup> secured the passage of a new Petroleum (Production) Act which had the effect of nationalising all onshore oil deposits. Uncertainties about property rights were, it claimed, acting as a barrier to exploration and so such a drastic step was necessary. No provision for compensation payments was included even where subsequent exploration might show the presence of large deposits under someone's land. The Act retained the licensing system and elaborated it by the promulgation of model clauses. As Professor Daintith notes:

The main provisions of this Act, relating to the vesting of petroleum in the Crown, the issue of licences, and the promulgation of model clauses, are still in force and have not been amended.<sup>2</sup>

The relationship between the State and licensee established

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1. T.C. Daintith, Proceedings, op.cit., at p.4.3.

2. loc.cit.



by the 1934 Act differs radically from the 1918 Act. The licence envisaged in the 1918 Act was like an 'administrative permission',<sup>1</sup> similar to a dog licence or a cinema licence. It was not without value since it conferred an exclusive privilege but did not give any property rights in oil to the licensee. By contrast, the 1934 Act added to the exclusive privilege conferred by the licence an element of transfer of property rights. Thus, the licence operates to transform the property of the Crown in any oil in situ into the property of the licensee in oil at the wellhead. Whether or not the licensee has any property in the petroleum deposit in situ and at what point the transfer of property takes place are different questions which I shall deal with later. The essential point here is that the licence serves as a vehicle for a transfer of property, remunerated by a royalty. Some of the Crown's rights are 'conceded' to a private party. The grant of a licence has the character of a commercial transaction and has always been considered a contract between Crown and licensee. However, these licences resemble the type of licence issued under the 1918 Act in possessing a regulatory character, effected through the model clauses, included in each licence. These cover most of the specialised rules relating to petroleum operations.

It should be stressed that the 1934 Act was not intended to provide the basis for a state petroleum industry: private companies were to do the actual operating. There were two overriding objectives:

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1. Cf. Manual: the licence may be 'legally analysed as administratively granted exemptions from legislative prohibitions' (p.26).

1. to displace obstacles to private exploration and production created by uncertainties about property rights in the deposits;
2. to organise and control exploration and production through the licensing regime so as to avoid competitive drilling.<sup>1</sup>

As it happened, no major oilfields have ever been discovered under the UK mainland or territorial waters.<sup>2</sup> Since 1934 a mere 362 exploration and appraisal wells have been drilled and yet total onshore oil production per day is only 0.17% of the rate from offshore production.<sup>3</sup>

The main significance of the 1934 Act does not, however, lie in its application to onshore exploration and production, but rather in its extension to areas outside territorial waters in which international law recognised in the UK rights to the sea-bed and subsoil and their natural resources. I discuss the manner in which this was done in chapter two. At this point it is sufficient to note that no substantial modifications were made to the regulations contained in the model clauses: the main changes were made in the mode of licence allocation. To this day offshore oil production is principally regulated by the terms of licences incorporating model clauses similar to those made under the 1934

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1. T.C. Daintith and I. Gault, op.cit., p.28.

2. Property rights in petroleum in the bed of the territorial sea are vested in the Crown not by the Petroleum (Production) Act 1934 but at common law. It should be noted that small oilfields have been discovered onshore and because of their cheaper cost can be quite profitable: for example, the Wytch Farm field in Dorset.

3. 'Why onshore exploration has been so slow-moving in Britain', in The Times, January 14, 1980.



Act. Many of the important elements of current UK policy and regulation were already reflected in the early provisions: for example, the device of a negotiated work programme as a stimulus to exploration and a guarantee of applicants' competence; in addition, elements of economic control of operations through restrictions on assignment of licences, on the disposal of production outside the UK, and compulsory unitisation of operations where the same field underlies adjoining licensed areas.

It is little short of remarkable that the main vehicle of regulation of exploration and production of oil from the UK continental shelf should have been licences which contained regulatory elements little changed since 1935. However, this dependence upon regulation under contractual forms was to lead to a 'crisis of legality' in 1974-5 when the Labour Government wished to make considerable changes in the licensing regime.

#### 4. Ownership of North Sea Oil<sup>1</sup>

In several important ways the development of North Sea oil is subject to state control, in spite of the involvement of large private oil companies in its extraction. The vesting of all rights exercisable over petroleum in the Crown was done through the Continental Shelf Act 1964. Private companies are allowed to explore for and exploit petroleum only after being awarded a licence in one of the licence 'rounds' held at periodic intervals. Each licence contains a number of detailed regulations in its model

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1. The North Sea is by far the most productive sector of the UK Continental Shelf and while much of what follows applies to the shelf as a whole it is the North Sea alone which concerns me in this study.

clauses which, inter alia, restrict a licensee's ability to assign his interest and provide for compulsory unitisation.<sup>1</sup> The licensee does not have property rights in the oil in situ; only once the oil reaches the wellhead does he have title to it, and even then the state oil company, ENOC, has a right to 51% of the oil produced from most fields.

Much of this state control was introduced unilaterally in 1975 through the Petroleum and Submarine Pipe-lines Act once the real extent of oil reserves became known. In this respect the action of the British Government in revising the terms of current licences resembles that of most producing states. The similarity was increased by the nationalist rhetoric of the then Labour Government, which accused its predecessors of having 'given away' a potentially valuable NATIONAL asset. Whatever grounds there were for doubt about the real extent of the Crown's proprietary control over the development of North Sea oil, these were removed after 1974, or so it seemed.

Nonetheless, the origins and the form of this 'social control' show just how limited it is and has to be. I have shown in section one how the special characteristics of oil (its fugacious character, exhaustibility, and difficulty of access) make a system of full private ownership both inefficient and socially undesirable. The origins of onshore licensing in the UK, as I sketched them in the last section, showed how recognition of this factor and fears about national security led to the nationalisation without compensation of onshore deposits of petroleum: a course favoured by at least

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1. Unitisation is a technique developed in the US to avoid wasteful exploitation of oilfields in which there subsist a number of separate proprietary interests, whether of mineral owners, lessees, or, as in Britain, licensees. The holders of the separate interests agree, or are required, to exploit the field as a single unit, and to appoint a unit operator for this purpose.



one oil company. However, all this regulation was done on the assumption that it would not prejudice the efforts of private oil companies to explore for and extract any oil that happened to exist. This applied both to onshore and to offshore deposits.

Admittedly, the extension of the licensing system was done with one major innovation in Government policy on regulation: a discretionary mode of licence allocation was adopted. Petroleum licences covering 'blocks' of sea-bed could only be applied for by invitation in the course of licence 'rounds' held at whatever intervals the Government thought necessary. One of the objectives of this system was certainly to encourage all licensees to carry out their exploration work as vigorously as possible,<sup>1</sup> but another one was to allow discrimination against some applicants in particular: American companies. It functioned as a means of reducing their inevitable dominance in the North Sea, given their greater capital resources and experience. It allowed discrimination in favour of British companies and increased 'British' ownership of any oil reserves: whether such ownership was public or private was less important than the fact that specifically British companies would be in control of it. We are not therefore viewing state regulation of private companies but more specifically the maximisation of British private companies' involvement in a potentially very profitable branch of production. Of course, discrimination in favour

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1. Applicants had to produce work programmes for the desired blocks and evidence of their ability to carry them out. This is discussed in chapter two.

of public sector companies like the British Gas Corporation (BGC) and the BNOC has also been common: this represents, as we shall see in chapter four, a simple attempt to ensure security of oil supplies in the event of a national emergency.

It should be noted that this discrimination through the mode of allocation did not involve simply ensuring that British companies received particular licences. Most licences are granted to consortia and not to a single company. Companies agree to work in a joint venture and thus reduce the element of risk and the capital cost of offshore drilling and development. The companies concerned appoint one of the consortium's members, usually an oil company, as Operator, to organise and supervise the work of drilling and extracting. For example, Shell is the Operator in the Brent, Dunlin, Cormorant, Fulmar and Auk fields. The system of joint venture encourages American consortia to invite British companies to join them and thus improves their chances of success in applying for licences. This theme of rivalry between British and American interests in the North Sea is one to which I shall return later.

A further kind of discrimination occurred over size. This was one of the few major areas of difference between Labour and Conservative Party oil policies. Successive Conservative Governments have favoured the involvement of small British companies in offshore consortia and expressed this preference in two of the largest rounds in 1964 and 1971-2 with the result that hundreds of small British companies became involved in North Sea oil

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activities. Considerations of efficiency would have led to a preference for the large companies and this has been the choice of governments in Norway and Labour Governments in Britain. One consequence of involving so many small companies was that much uncertainty was created in 1974-6 when they had great difficulty in meeting the cost of their contribution to field development.

However, much of this state regulation is of recent origin, and, as I have shown in the previous sections, it has tended to be facilitative. In other words, some kinds of state regulation have been necessary to permit private economic activity on a significant scale. Alternatively, and more recently, it has been designed to ensure that the development of oil has corresponded roughly to the interests of British capitalism as a whole (taxation, security of supply, etc.). It should not be interpreted as an attempt to control the anti-social activities of oil companies or to curb abuses of private power. It may be so interpreted but, in so far as this element exists at all, it is only an incidental function of the body of legislative rules.

Indeed, a methodological comment may be made at this point. To the extent that one limits one's focus solely to the legal rules concerning petroleum licensing in the UK, a picture will emerge of capitalist activity which is highly regulated by the state and of state regulation which has increased dramatically from 1975. This does not preclude consideration of the role of discretion

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and of policy, and is the kind of view found in the work of Daintith and Willoughby, for example.<sup>1</sup> Such a view has the effect of masking the real dominance of the private oil companies and of exaggerating the element of autonomy which the state, and especially the advanced capitalist state, has from those private interests. By adopting a broader perspective, admitting certain 'social facts' usually considered the subject-matter of political science or economics, quite different conclusions result. For example, if we admit (and few would not) that the real power of the oil companies extends far beyond the legal powers they have as licensees, and includes control of capital or means of production and in this case exploration too, an analysis of the licence itself becomes much less important for an assessment of state regulation. Indeed, an understanding of the licences themselves will become quite impossible unless some examination is undertaken of the various forces which produce petroleum licences. In other words, instead of beginning our investigation of licence rights with a study of the licences themselves, we should begin with a study of the various social, economic and political forces which give rise to petroleum licences. I have adopted this approach in the first three sections of this chapter to explain why private ownership of oil resources, as opposed to

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1. Manual op.cit. See also various contributions to the Energy Law Seminar at Cambridge, September 29 - October 4, 1979 (Proceedings, IBA): (volume 1) Bernard G. Taverne, 'Concessions and New Types of Exploration/Production Contracts' (Topic H, Paper 1); (volume 2) Michael H. Elliott, 'Comparison of Terms to Attract Petroleum Development in Four Countries: the United Kingdom (Topic Q, paper 3); Rosalyn Higgins, 'Ten Years of State Involvement in the Petroleum Industry: the United Kingdom (Topic R, paper 1).



concessionary or contractual arrangements, has become less and less favoured by producing and consuming states, as well as by the oil companies themselves. Without in any way minimising the impact of OPEC's role in the international oil industry, I have suggested that company profitability need not be significantly affected by alterations in the legal arrangements for the development of oil resources which gives the state a greater regulatory and even participatory role.

Once we have noted a methodological tendency in some approaches to exaggerate the implications of state regulation and the absence of private ownership of the resource in situ, the question remains, whether or not the difference in legal form between licence rights and property rights really matters. Is it to be explained away By referring to socio-economic factors? Can we, without more ado, simply describe some or all licence rights as property rights in the pragmatic manner favoured by economists like MacKay and Mackay,<sup>1</sup> dismissing the difference in legal form as a mere 'legal fiction'?

In one sense there clearly is a difference: the rights conferred by a licence (rights L) cannot be identical to rights of property (right<sup>SP</sup>) because L means something different from P. Nonetheless, we can argue that rights L have the same socio-economic consequences for the holder of those rights as do rights P for their possessor. In this way the difference between the two is minimised and this is how I argue in the following study. However, it is not my intention to avoid the question altogether.

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1. D.I. MacKay and G.A. Mackay, 'The Political Economy of North Sea Oil'. But see also Dam, Oil Resources, chapter 17.

I do attempt to show that the difference in legal form has some significance: practically, by rendering the licensee's rights more or less uncertain relative to the state than those of a property owner and leading to a network of legal or extra-legal techniques designed to minimise that uncertainty; and theoretically, by supporting a thesis advanced by Pashukanis that law and political power exist in an antithetical relationship to one another. This latter concern with the implications of the difference in legal form between licence rights and property rights will be an important theme throughout this study. In addition, it has a political significance which should not be underestimated. The idea of petroleum as a resource which 'belongs' to the nation has been common in the UK for decades, but with the discovery of large quantities of petroleum offshore and Britain's entry into the EEC, the idea has acquired a new significance. The juridic concept of property in offshore oil has an ideological connotation, in the sense that it serves as an expression of the primacy of a national interest over all other national interests and over any particular interests, especially those of oil companies, many of which will be foreign-owned. It thus serves to legitimate a specific relationship between oil companies and the British state. The validity of this use of the concept does not concern me here: I only note that it does have this ideological connotation.

In these preliminary remarks about the ownership of North Sea oil I have argued that ownership of oil resources is bound up with

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ownership of the capital resources required to explore for them and to extract them. The extent to which the latter leads to a de facto ownership of oil resources can be masked as a consequence of the choice of a particular methodology, or neglect of the real links between some states like Britain and the USA with the principal holders of capital for oil development. Adoption of a historical approach to the development of law and policy on petroleum licensing helps to bring out the degree of private dominance in oil development in the UK, and for this reason I have adopted such an approach in the following three chapters.

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## CHAPTER TWO

### Oil Companies and the State, 1960-1974



Hitherto the sea has been treated as primitive tribes treat the jungle or prairie - for hunting or gathering food. But on the continental shelves alone a rich continent the size of Asia waits to be mined and farmed.<sup>1</sup>

1. Petroleum Press Service, Down to the Sea Bed, August 1965, p.289.

**Contents:**

1. The legal framework
2. Licensing and state regulation
3. State participation: the nationalised industries
4. The crisis of legality



## 1. The Legal Framework

Oil companies first became interested in the North Sea as a potential source of petroleum in 1959, when major fields of natural gas were discovered at Groningen, a province in the N.E. Netherlands. This discovery was sufficiently large to be classified as 'major' by world standards. As much as 1,100,000 million cubic metres of natural gas was thought to exist there.<sup>1</sup>

Geologically, the Netherlands belongs to a sedimentary basin the centre of which lies in the North Sea and also covers some of the other surrounding countries, including Denmark and N.W. Germany. It seemed very possible that conditions similar to those at Groningen might be present under part of the North Sea. Once the possibility of potentially rich petroleum-bearing strata under the continental shelf was established, the high cost of offshore exploration was removed at a stroke as a prohibitive factor.<sup>2</sup>

The most attractive feature about possible oil and gas discoveries was their location within 300 to 700 miles of one of the most densely populated industrial regions in the world. The North Sea was on the doorstep of some of the world's largest markets: for example, in 1960, the U.K. was the non-communist world's biggest oil consumer, after the U.S.A. and Canada. The transportation costs would therefore be low, and the task of finding market outlets easy to solve.

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1. 'Rush to the Sea', in Petroleum Press Service, June 1963, pp.211-13.

2. The dominant assumption was that any petroleum found would be in the form of gas. Until the late 1960s, oil was not thought to exist in large quantities in the North Sea.

Nonetheless, the continental shelf had not been more than sketchily explored and a programme of preliminary surveys was necessary before its prospects could be assessed.

The proximity to Western Europe had another advantage: a strategic one. Throughout the period following the Second World War nationalism was a growing force in the Middle East. Relations between the oil companies and the governments of producing countries had become increasingly strained, culminating in the formation of O.P.E.C. by oil-producing states in 1960. The objectives were to present a collective front against the international oil industry, and to secure a greater control over their product and the rent accruing from its sale. Although for many years a weak organisation, its establishment in 1960 added to company fears for the long-term profitability of their operations. From their point of view, the location of alternative sources of supply to reduce their dependence on the Middle East was a sensible, though not urgent, task.<sup>1</sup> The North Sea appeared a distinctly safe political environment by comparison with the Middle East. Most West European governments did not, for instance, treat oil as a public utility (unlike gas), and private companies therefore had considerable freedom to produce and benefit from the resource.

Nonetheless, there is a risk of rereading history in the light of subsequent events. At this stage (1960-3) no-one, including the oil companies, could have predicted the speed with which O.P.E.C. gained the power to set world oil prices, or the suddenness of nationalisation measures in the Middle East. The context was one of a

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1. BP was an exception: its heavy dependence upon the Middle East for supplies of crude oil dictated a policy of diversification of sources of supply. Since the early 1960s when it was a 'crude-long' company, with much crude oil in supply but few distribution facilities, it has diversified its sources faster than the other majors, acquiring large interests in the North Sea and the U.S.A.



continuing abundance of cheap oil from the Middle East, to be supplemented by new oil and gas discoveries in North Africa; and for which easy markets could be found in Western Europe. Apparently, the North Sea discoveries and their implications 'went largely unremarked' by 'policy-makers' who

were more concerned with protecting their declining coal industries from the existing flood of cheap oil imports which the integrated oil companies ... were pouring into the continent.<sup>1</sup>

The third reason for oil company interest in North Sea exploration concerned competition. Large quantities of oil had been discovered with the American market in mind, but they had been excluded by the introduction of a quota system by the United States Government in the 1950s. Several oil companies were therefore compelled to move into the West European market to sell oil they had originally planned to sell in the United States. The competition between the majors (e.g. Esso, Shell) and the 'independents' (e.g. Occidental) was 'the most important single factor in ~~making the~~ European oil system so competitive in the 1960s'.<sup>2</sup> There was a competitive advantage to be gained in conducting preliminary surveys in the North Sea as quickly as possible. The geological data thus acquired would be of much value when companies came to apply for production licences at a later stage.

A final reason has been suggested by Peter Odell. The oil companies, he claims, did not think that any oil or gas found in the

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1. L. Turner, 'State and Commercial Interests in North Sea Oil and Gas: Conflict and Correspondence', in Saeter and Smart (eds.), *The Political Implications of North Sea Oil and Gas*, p.93.
2. P.R. Odell, 'The Economic Background to North Sea Oil and Gas Development', in Saeter and Smart, op.cit., p.74.

North Sea would represent a threat to the status quo.<sup>1</sup> It was generally accepted that the amount of oil available from the North Sea would be small relative to the total Western European demand in future. Any oil found in the North Sea would provide a small but useful addition to Western Europe's indigenous energy supply. It would not, however, be so productive as to replace traditional sources of supply: that is, the Middle East and North Africa. This was not only the expectation, but it was also what the oil companies wanted. Relative to cheap oil from traditional suppliers, the high cost oil from the North Sea was not attractive but this merely reduced their interest in rapid exploration. It did not eliminate it altogether, since any oil from the North Sea could be integrated into the existing infrastructure for foreign oil without any major difficulties. What the oil companies wanted above all was

a build-up of knowledge of the North Sea potential together with the opportunity to experiment with offshore drilling and field developments in deep water - in preparation for their expectation of an increasing need for such offshore oil later in the century.<sup>2</sup>

By 1963, many oil companies had made clear their interest by conducting preliminary surveys in the North Sea. In spite of natural barriers to exploration (the bad weather restricted operations to the summer months alone), the number of companies engaging in exploratory work increased to more than 40 in 1964.<sup>3</sup>

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1. Odell, op.cit., p.53.

2. Odell, op.cit., p.53.

3. 'Rush to the North Sea', op.cit., p.211.



The U.K. coast was the base for the most active exploratory operations in the North Sea. The unusual character of this 'rush' was commented on by one industry journal thus:

The decision of so many companies, at one and the same time, to take a stake in the North Sea search is reminiscent of what usually happens when governments suddenly invite applications for prospective oil lands under more or less favourable legal conditions.<sup>1</sup>

An example of this was Libya before Gaddaffi's seizure of power. However, the considerable interest in the North Sea was not due to the adoption of a generous oil law, but to a re-evaluation of the geological potential and the economic costs.

Nonetheless, the economic activity had a definitely provisional character, being confined to seismic surveys and other work of a preparatory kind. It was unlikely that exploration wells would be drilled until a legal framework was provided, since otherwise there was insufficient security for individual company interests from encroachment by other companies or consortia, or, less likely, by another nation-state. The problem was outlined by one industry journal thus:

At present, if oil and gas were discovered, it is doubtful whether the governments of the North Sea countries would be able to protect the original operators and prevent others from rushing in and exploiting the new resources on their own. Also such finds could lead to territorial disputes among the North Sea countries themselves.<sup>2</sup>

The high cost of exploratory drilling underlined this point. While

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1. loc.cit., p.211. However, rapid exploration by the large oil companies in offshore areas was common in the 1960s, in spite of an oil glut. Hamilton interprets this as evidence of their Faustian drive for more and more oil, in C. Tugendhat and A. Hamilton, Oil, the Biggest Business, p.352. More realistically, Chapman claims that the speed of development in the North Sea has been mainly due to 'fundamental political and economic forces that are themselves ultimately based upon the world geography of petroleum production and consumption': North Sea Oil and Gas, p.8.
  2. 'Rush to the Sea', op.cit., p.213, my emphasis. It was also suggested in this journal that preliminary activities had ceased in some cases because a legal framework was lacking (in June, and October 1964 issues).

survey activities could be carried out relatively cheaply, one test well could cost (at that time) up to £1 million to drill in the North Sea.<sup>1</sup> Plans might be made to commence drilling operations but investment on the required scale was unlikely to be made until some legal guarantee existed that it would not ultimately benefit other (competitor) companies.

A legal framework was not only necessary, it also had to be introduced as soon as possible. The 'uncertainty' about legal conditions was, it seems, inhibiting test drilling in the North Sea.<sup>2</sup> Since such drilling could only take place in the summer months, it was essential to remove the obstacles to this in time for the drilling season in the summer of 1965.<sup>3</sup> Furthermore, the more aggressive companies were concerned that failure to introduce a system of licensing and allocating 'blocks' at the earliest opportunity might allow their slower competitors to erode the advantage they had gained in collecting and evaluating geological data, to be used when licences were eventually allocated.<sup>4</sup>

The first step in the provision of a legal basis of offshore exploration was taken in 1964 with the passage of the Continental

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1. 'N.Sea Rush Gathers Force', in Petroleum Press Service, May 1964, pp.164-7.

2. loc.cit.

3. Weather conditions originally prevented drilling in the winter months. However, technical progress was so rapid that by December, 1964, it was assumed that operations would go on through the winter months.

4. L. Turner, in Saeter and Smart, op.cit., p.94.



Shelf Act. This had two principal effects: firstly, it amended U.K. law to allow implementation of the Continental Shelf Convention and secondly, it extended the licensing provisions of the Petroleum (Production) Act 1934 to the area beyond territorial waters.

Ratification of the Geneva Convention removed the uncertainty surrounding the basis in international law of oil exploration in the North Sea outside territorial waters; it also brought the Convention into force. While it already had some customary legal validity, it could not come into force until ratified by a minimum of 22 states: the U.K. was the 22nd state to do so.

Under the Act 'any rights exercisable by the United Kingdom outside territorial waters' were assigned to the Crown.<sup>1</sup> There is, however, no specification of the nature or extent of these rights. To the extent that 'sovereign rights for the purpose of exploring ... and exploiting'<sup>2</sup> are granted to the state by international law, the Crown has property in the resources of the seabed and subsoil, although their precise legal character is not entirely clear. J.P. Grant suggests that the use of 'sovereign' in the Convention is political rather than legal since the actual rights conferred on States under the Convention are not identical with the normal sub-divisions of territorial sovereignty into 'dominium'

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1. The Continental Shelf Act 1964, s.1(1), excepting rights in relation to coal (see subsection (2)).

2. Convention on the Continental Shelf, Art. 2, para. 2.

(the ownership of territory) or 'imperium' (the exercise of governmental powers), particularly with the former.<sup>1</sup> The coastal State does not own the shelf but has merely an exclusive right to the resources of the shelf: such a right is exclusive in the sense that

If the coastal State does not explore the continental shelf or exploit its natural resources, no one may undertake these activities, or make a claim to the continental shelf, without the express consent of the coastal State.<sup>2</sup>

Furthermore, the rights

... do not depend on occupation, effective or notional, or any express proclamation.<sup>3</sup>

In addition, the coastal State cannot exercise full governmental powers over the shelf, but only such particular powers as the Convention permits and which are necessary for the enjoyment of that exclusive right. The Act makes it clear that the shelf regime is not assimilated to the State territory. It merely provides the means by which the UK could make claims to a continental shelf area, although it did not specify the extent of the claims.<sup>4</sup>

Given these various characteristics, can we describe these as rights of ownership of petroleum in the ground? Although the answer to this question is not clear, the lack of clarity has not given rise to any difficulties in practice. There is also a sense in which the question is a red herring. In international law there is

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1. In Manual, p.172.

2. Convention on the Continental Shelf, Art.2, para.2.

3. Convention on the Continental Shelf, Art.2, para.3.

4. Cf. Manual, p.172. With respect to the objects of those rights: under Art.2, para.4, a coastal State is entitled to explore for and exploit all mineral and non-living resources on or under the continental shelf. It is not entitled to the fish swimming in the waters above its continental shelf (cf. Manual, p.173).



certainly an important practical difference between 'sovereignty' (over territory or territorial waters, for example) and 'sovereign rights' to which the Convention refers.<sup>1</sup> However, from the point of view of municipal law, the words in the Act can be taken simply as delimiting and characterising the rights which the Crown has. Does the Crown by 'having' these rights 'own' anything? Indeed, it does. It 'owns' the resources of the seabed and subsoil to the extent that sovereign rights over them are granted to the State by international law.

None of the above is modified by the ideological use to which 'ownership' has been put vis-à-vis North Sea oil since 1964. The relationship of the Crown to the resources in situ has been described by members of British Governments and in political party documents as one of 'ownership'.<sup>2</sup> By contrast, during the passage of the Continental Shelf Act, a government spokesman asserted that the Crown did not have rights of ownership of petroleum in situ.<sup>3</sup> Daintith and Willoughby designate this latter view as the 'official view',<sup>4</sup> since it reflected the prevailing interpretation of the

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1. The distinction has become much less important since 1964, particularly after the North Sea Continental Shelf Case [1969] 41 ILR 29. ICJ Rep 3; 41 ILR 29.

2. For example, 891 HC Deb., col. 485 (April 30, 1975), and Labour's Programme 1973, at p.32: 'We will bring North Sea oil into public ownership and control', to which the White Paper responded in July 1974: 'Britain's oil is of course already publicly owned. Public ownership was established by the last Conservative Government but one under the Continental Shelf Act 1964' (Cmd. 5696) (at p.3).

3. HC Deb. Standing Committee A, col.19 (February 12, 1964), cit. in Manual, p.232.

4. Manual, p.232.

position in international law. However, changes in international law since that time have changed this somewhat,<sup>1</sup> and, in addition, the dominant assumption made by Governments in recent years has certainly been that the concept of 'public ownership' is applicable.<sup>2</sup>

The second principal effect of the Act was the extension of the licensing provisions of the Petroleum (Production) Act 1934 to the area beyond territorial waters. The Geneva Convention had left the details about licensing arrangements to individual States. As a Convention among States (persons in international law), it was concerned to allocate rights in international law to the States themselves. What the States did with them was their own affair. Legislation was therefore a necessity imposed by municipal law and the British Government did this by extending the licensing provisions of the 1934 Act over the continental shelf. This was supplemented by Regulations which set out the procedure by which the Minister of Power would award licences.<sup>3</sup>

The almost casual way in which this legal framework was established seems quite remarkable. Preparations were left almost entirely to one Department, the Ministry of Power. Consultations took place with other Government Departments and with two committees set up by interested oil companies. These covered legal matters,

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1. In particular, the North Sea Continental Shelf Case 1969, which suggests that the term 'ownership' is now applicable.
  2. For example, the concept is implied by statements made by a Conservative Minister, Lord Drumalbyn, at the time of Britain's entry into the EEC: 336 H.L. Deb. (November 22, 1972) at col.1019, and 346 H.L. (Oral Answer) (November 15, 1973) at col.751: 'The Government have made it clear that North Sea petroleum is a national asset in the same way as oil and gas and other minerals found on land in the United Kingdom', and 'there is no doubt that the ownership is national. What happens is that a licence to exploit is granted to various licensees' (col.752). See also Lord Carrington's assurance that 'North Sea oil belongs to us' (348 H.L. (Oral Answer) (January 21, 1974) at col.1189).
  3. The Petroleum (Production)(Continental Shelf and Territorial Sea) Regulations 1964.



technical and operational subjects. The Institute of Petroleum provided technical advice, and the TUC and the Institute provided advice on safety, health, and welfare of employees of licensees.<sup>1</sup> In November, 1963, a Bill was introduced into the House of Lords by a Conservative Government. However, it was not treated as an especially important piece of legislation, and obtained a place on the parliamentary agenda only when another Bill had dropped out.<sup>2</sup>

The lack of imagination was remarkable. Despite the various consultations, the legislation to apply to offshore territory was in many respects identical to that applying onshore. 'Special' legislation for oil exploration and production was clearly not considered necessary. One consequence of this procedure, and of the apparent aversion of policy-makers to making specific legal rules in this case, was the absence of any re-negotiation clause in the licences themselves. As we shall see, the only way a Government could revise the terms of licences once allocated, should there be significant discoveries, was to take unilateral action, which raised the question of legality. Ironically, in spite of the comprehensive legislation since 1974, introducing new licence regulations, a unique taxation system and a national oil company with an extensive range of activities, there is still no re-negotiation clause.

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1. PAC Report, para.13 p.ix. For See C. ...
  2. Interview with Mr. Angus Beckett. Lord Balogh later described it as 'one of the most amateurish productions of the then Ministry of Power', in A UK Socialist View of North Sea Developments, Financial Times Conference, 1972, pp.110-13.

The final step in providing a secure legal framework was to resolve any potential delimitation disputes with neighbouring States. While this is not a once-and-for-all matter, there was one delimitation problem at that time which had to be resolved as soon as possible if exploration in the North Sea were to be quite secure: the borderline between UK and Norwegian sectors.

The <sup>boundary</sup> frontier of sovereignty <sup>the continental shelf</sup> between various coastal States was, according to the Geneva Convention, the median line between them, but in the case of North Sea States, it proved necessary for States to reach agreements between themselves to demarcate their respective zones at an early stage of exploration.<sup>1</sup> These delimitation agreements were an essential part of the provision of legal security for the operating companies and were essential if certain borderline territories were to be allocated for exploratory activity at all. The UK State reached such an agreement with Norway with remarkable speed, given the potential for dispute.

The existence of a trench on the seabed separating Norway from the Continental Shelf rendered the extent of the Norwegian shelf unclear, and Norwegian doubts about the effects of the Convention in the light of this geographical peculiarity persuaded it against ratification: a dispute arose between the two Governments. On one interpretation of the Convention, the country was not entitled to any significant share in the open sea.<sup>2</sup> The British Government

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1. The Convention on the Continental Shelf, Art.6, para.1.

2. For fuller discussion of this, see E. Young, Offshore claims and problems in the North Sea, 59 A.J.I.L. 505, 506 (1965) and the references cited there.



settled this dispute in 1965, but only at the cost of forfeiting any claim to part of the North Sea which it might well have acquired if the dispute had been submitted to international arbitration. The territory gained by Norway was later discovered to contain the Statfjord oilfield, one of the largest in the North Sea. The speed with which the Government reached agreement on the Norwegian Trough is explained by the policy of rapid exploration. The Government was anxious to remove all obstacles to this goal.

The cavalier attitude to one small part of the North Sea is perhaps easier to understand when one considers the size of territory to which the UK was entitled under the provisions of the Convention. Since the UK forms the western boundary of the North Sea over a length of some 500 miles, it was therefore allowed control over nearly one half of the North Sea area including much of its most promising structure. The UK sector covers about 100,000 square miles, and is roughly equal in size to the combined sea areas belonging to four other North Sea countries: the Netherlands, West Germany, Norway and Denmark. The UK sector of the North Sea was by far the biggest.

To sum up: by 1964, the means for and the interest in offshore exploration in the North Sea existed. The absence of a legal framework acted as an obstacle to that exploration. To remedy this, it was first necessary to establish a legal regime which firmly vested in the UK State rights over the seabed and subsoil, and

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secondly enabled the State, by virtue of those rights, to confer on private companies rights of extraction of petroleum by means of a licensing system. The State is then enabled, by virtue of its right, to confer extraction rights on others. The Continental Shelf Act established a legislative framework within which, subject to further exercises of State power (by way both of delegated legislation and of licence granting), the companies' operations could be carried out. Finally, the principal delimitation dispute with Norway was resolved.

## 2. Licensing and State Regulation

The initial assumption of 'ownership' by the State was designed to overcome specific barriers to economic activity like the adverse effects of unfettered competition between private companies, each possessing or having access to the technology required for exploration. This did not exhaust the State's role however, since the system of licensing was not designed merely to transfer exclusive rights to whichever companies wished to explore for oil and gas. There were at least three other objectives which the licensing system was designed to achieve. These were:

(1) Discrimination in favour of British applicants. The method of allocation was discretionary in order to discriminate in favour of British companies which applied for licences. This was not an unusual choice, and was also chosen by the Dutch.<sup>1</sup>

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1. For an official statement of this objective, see para.8 of the Memorandum submitted by the Department of Trade and Industry to the Public Accounts Committee; op.cit. p.25. For discussion of this see Kenneth W. Dam, Oil Resources, pp.25-6, and pp.40-1; and Keith Chapman, North Sea Oil and Gas, pp.94-5.



(ii) Intensive exploration. The idea of a work programme was introduced which would commit a licensee to carry out a specific amount of work. This was designed to exclude inefficient applicants and also those whose principal goal was to 'sit' on the block or blocks until they had appreciated in value to the extent that a profit could be made on disposal of the interest.<sup>1</sup>

(iii) Securing the maximum share of the rent. This would be a valuable source of additional revenue for the state, and could be obtained in various ways, like taxation, state participation, or royalties. Balance of payments deficits would also be ameliorated by revenue from this source.<sup>2</sup>

The overtly 'nationalist' aspect of the licensing system lay in the method of allocation by discretion. The international oil economy was dominated by American-owned oil companies, and it was considered vital to regulate their inevitable entry into North Sea exploration activity. An official view expressed the problem thus:

Although it was recognized that American oil companies would inevitably play a major part because of their numerical superiority, technical expertise and ownership of or ready access to the equipment needed for off-shore drilling, it was considered essential that British interests should be well represented.<sup>3</sup>

The discretionary mode of allocation seemed to resolve the problem.

Private companies wishing to explore for oil and gas had their

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1. PAC Report, para.16 pp.x-xi; Memorandum, op.cit. paras.8 and 11, pp.25-6. The work programme is discussed in Dam, op.cit. pp.34-6, and Chapman, op.cit. pp.92-3.
2. PAC Report, Memorandum, paras. 6-7, pp.24-5.
3. PAC Report, para.16, pp.x-xi; the possibility of discriminating against American oil companies is given as one major reason for preferring the discretionary to the auction method.

applications for licences examined by a Government Department and evaluated according to several general criteria.

The regulations made under the 1964 Act instituted arrangements whereby seaward areas were divided up into blocks of an average size of 250 square kilometres. Licence rights for these blocks were to be allocated in 'rounds' of licensing in which applications would be invited for a specific number of blocks 'offered': the timing of such rounds was subject to the Minister's discretion. The size of these blocks proved a source of some controversy: most of the oil companies favoured larger blocks than those chosen by the Ministry of Power in 1964. The decision about size was, however, bound up with the 'nationalist' factor. The Ministry wished to involve as many British companies as possible, to the extent that it encouraged smaller British companies to form consortia and hence become eligible as applicants for blocks.<sup>1</sup> It was obviously easier to involve smaller companies in this way if the blocks were smaller. In addition, the larger the number of blocks available, then the less likelihood there was of disappointed applicants.

The blocks were allocated by the Ministry<sup>2</sup> among the competing applicants by reference to general (and extra-statutory) criteria which remained similar for each round. The basic elements in the criteria were these: the financial and technical capability of applicants, their previous licensing experience and exploration

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1. Interview with Angus Becket, also interviews with George Williams, chairman of UKOOA, and Roger West, senior executive in the Gulf Oil Company.
2. Initially, licensing was the responsibility of the Ministry of Power, changed to the Ministry of Power and Technology from 1967-1970, and then the Department of Trade and Industry from 1970 until the creation of the Department of Energy in 1973.



work, their contribution to the British economy, and, where foreign companies were concerned, fair treatment by their Governments of British applicants in their territories.

In the first round, the most valuable blocks attracted a concentration of applications which left wide scope and much need of the power of discretion. Of course, the relative value of the various blocks was not a matter of certainty at that stage: areas like that lying opposite the Dutch natural gas discoveries at Slochteren were perhaps exceptions. Where such a concentration of applications existed, the obligation to submit a work programme for the blocks applied for showed its significance. Applicants for widely sought after areas were obliged to upgrade their programme or drop out. An element of auction entered here in the comparison of the work programmes proposed by applicants for the first period of the production licence: 'the bigger and better the programme, the greater the chance of success'.<sup>1</sup> Apparently, a 'going price' came to be known for each area. This was denominated in such things as holes drilled and exploration work undertaken. Whoever was ~~compelling~~ to pay this could not expect to be awarded a licence. Where an applicant's programme of work for a particular block was deemed insufficient to the Ministry, he was informed that unless he increased the level of exploration and drilling activity promised he was unlikely to be awarded a licence for that particular area.<sup>2</sup> This bargaining process allowed the Ministry to introduce

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1. T.C. Daintith and I. Gault, Pacta Sunt Servanda, op.cit.

2. An account of this is given in Kenneth W. Dam, Oil Resources, op.cit. at p.28.

some competition into the work programmes. Once an agreement had been reached, the work programme became part of the licence obligations of the successful applicant.<sup>1</sup>

The use of discretionary power, a common characteristic of public law in Britain, was considerable here.<sup>2</sup> Comparing the various work programmes submitted by applicants was a task which required elaboration of the general criteria and a weighting or 'points' system was introduced to compare applications. A numerical weight factor was applied to each of the items included in the criteria, and the weightings

... represented the relative importance of the criteria in the matter of determining the suitability of applicants as potential licensees. They varied from company to company according to the extent to which the criteria were met.<sup>3</sup>

The details of this weighting system were not made public. When a House of Commons Select Committee inquired about this, it was not given examples of how the ratings worked in practice.<sup>4</sup>

However, it seems that during the first four rounds a high rating was given to participation by British companies in a licence and, in the second and third rounds, to participation by public sector companies.<sup>5</sup>

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1. It should, however, be noted that the work programme related to each licence and not to each block. Consequently, if the licence area was large, then the licensee would have greater flexibility in discharging his obligation.
  2. On general questions of legal control of discretionary powers such as these see de Smith, Judicial Review of Administrative Action, chapter 6.
  3. NISC Report, Appendix 19, p.251.
  4. Appendix 12, Answer 2(e), pp.233-4.
  5. loc.cit.



It is not suggested that this use of discretionary power is unusual, in domestic law, merely that it allows a Government to exert some influence on the capital and national composition of licensees, as well as the rate at which exploration takes place. Under s.2 of the 1934 Act, the Secretary of State's discretionary power is so wide that it

... should not be difficult to find, by reference to other criteria,<sup>1</sup> genuine reasons for deciding against the foreign applicant.

An unusual feature of the discretionary method of allocation concerns competition. The assignment of rights to the Crown by the Continental Shelf Act created a condition of scarcity. Private companies wishing to explore were dependent upon the state for rights to do so. Even if they had access to the necessary technology, only the state could provide and assure an exclusive right to conduct operations offshore. The possibility of competing private interests was replaced by the state's monopoly. However, an element of competition was reintroduced in the method of allocation. As we have seen, applicants were encouraged to compete with each other in the submission of work programmes for promising areas.

The result of the first round of licensing was that 53 licences were awarded by the Conservative Government to companies or consortia, including all the majors. The initial work programmes called for the expenditure of £80 million over six years. Consequently the combined enterprise of the various groups represented one of the largest ventures in oil industry history.<sup>2</sup> The licences varied from

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1. Manual, p.26.

2. For some interesting comments on this round see: '£80 million North Sea Search', in Petroleum Press Service, October 1964, pp.364-6.

one to ten blocks in size and, since each licence could cover a number of blocks and each licensee was allowed to receive a number of licences, the licences covered 348 blocks and the number of licensees was a mere 23.

The manner in which licences were awarded was the subject of some controversy: it was suggested they ought not to have been awarded so near to a General Election. The new Labour Government refused to alter them however in 1965,<sup>1</sup> and did not differ significantly in its approach in the second and third rounds. In order to increase the participation by British companies, the Petroleum Division of the Ministry of Power was active in encouraging the formation of British consortia to apply for licences (this of course included banks and insurance companies). This dirigisme seems to have increased the total British share from 25% to 35%.<sup>2</sup>

The second round was not significantly different from the first, and neither was the third one (with the exception of an emphasis upon state participation). However, by the time of the third round, in 1969, certain technological barriers to drilling in the deeper waters of the northern North Sea were surmounted with the consequence that vast new areas of the continental shelf became accessible to exploratory drilling.

### 3. State Participation: the Nationalised Industries.<sup>3</sup>

It is often forgotten that state participation was not a concept

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1. See 710 H.C. (Oral Answer), cols.222-4 (April 6, 1965), and 703 H.C. (Oral Answer), cols.225-6 (December 1, 1964): 'As these licences have already been issued the Government have concluded that it would not be in the public interest to disturb them' (Fred Lee, Minister of Power, at col.225).
  2. Interview with Angus Becket.
  3. Although the British Government held a majority shareholding in BP throughout this period, its relationship to Government is a unique one, giving it considerable independence: for that reason it is not considered here, (see chapter one, section 3).



foreign to actual North Sea developments during this period. Despite rejection of the scheme for a National Hydrocarbons Corporation, there was a form of state participation in petroleum development in the North Sea from the very beginning. This involved the British Gas Council at first (1965) and then the NCB.

Even in the first round of licensing, the public sector interest was 9.2%, and this grew to 15.5% in the second round.<sup>1</sup> Indeed, from the second round onward, the criteria for licence allocation were broadened to take account of proposals made for facilitating participation by public enterprise. A high rating was given to applicants who included such proposals in their plans.<sup>2</sup> The third round was far more important in this respect since new criteria were adopted, which stressed additional participation by the Gas Council and the National Coal Board. Preference was to be given to groups involving the Gas Council, the National Coal Board (NCB), and other British companies. It was also laid down that applications for licences in the Irish Sea should provide for participation by the Gas Council or the NCB through direct partnership or some other arrangement.<sup>3</sup>

There are several reasons for looking more closely at the form of state participation during this period. The late 1960s marked a

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1. PAC Report, p.89. This figure includes BP's interest.

2. NISC Report, pp.233 and 251. The 'rating' according to a system of weights in the discretionary award of licences is explained on p.108 of this chapter.

3. NISC Report, p.234.

turning point in North Sea developments. Gas deposits were discovered in 'commercial' quantities shortly after licences had been granted in the second round in November 1965. BP found gas in what became known as the West Sole field. Three other fields were discovered subsequently: Leman Bank, Indefatigable and Hewett, all in the southern part of the North Sea. At the same time, the Norwegian Government introduced a state oil company, Statoil, as part of an aggressive oil policy. The Labour Party too, as we have seen, was deliberating institutional forms which might maximise state participation.

One writer has claimed that the stress upon additional participation by the Gas Council (BGC) and the NCB can be fully understood only in the context of Labour Party internal politics, and that increased public sector involvement 'appeared to be a partial concession to views held by important segments of the Labour Party'.<sup>1</sup> The author is right to stress the link but draws the wrong conclusion. This form of participation was essentially conservative,<sup>2</sup> and was even advantageous to the oil companies involved.

To demonstrate its conservative quality, one must penetrate the ideological fog surrounding the notion of 'participation' itself. If we say that the state 'participates' in an activity, this implies that the activity remains primarily private (or, at least non-state). Yet the term conveys the notion that in some way

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1. K.W. Dam, Oil Resources, pp.29-31, esp. at p.31.

2. For discussion of degrees of participation which explains why this form was conservative see chapters one and four.



'the people' as a whole are involved, presumably to their advantage. There remains however a studious vagueness as to the degree of involvement or control. 'Participation' dodges the issues about control, while exploiting the favourable connotations of popular involvement in 'a good thing'. With these points in mind, let us examine the practice of state participation during this period.

In preference to the form of participation envisaged by the Fuel Policy Study Group of the Labour Party, the Government decided to encourage involvement of certain nationalised industries after the review of licensing in 1969. This involvement was not compulsory except in the Irish Sea, where it was to be obligatory for applicants to provide for participation through direct partnership or some other arrangement.

State participation of this kind could be considered 'successful' in the North Sea, since private companies were far from reluctant to invite either of these bodies to participate in their consortia. The preference given to applicants who promised to do so in the rounds of licensing undoubtedly had an influence upon American owned companies, like Gulf and Conoco, which proved especially enthusiastic to involve the nationalised industries in their plans.

Before we can understand the role taken on by the nationalised industries in 'participation', it is necessary to digress a little and make some remarks about the way companies operate in the North Sea.

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For the most part, exploration is carried out by oil companies which are transnational in character but largely American owned.<sup>1</sup> As a rule however, these companies have tended not to operate singly in the North Sea, but in consortia made up of more than one oil company often in partnership with other providers of capital who have no or only limited experience in oil-related developments.

There is nothing unusual about these 'joint ventures', as they are called: in fact, the formation of consortia is a common practice in the oil industry. They are to be found throughout the world in the development of oil and gas fields, and have been described as 'the standard worldwide practice'.<sup>2</sup> Even the biggest companies like Shell and Esso conduct operations in this way.

The legal form of such joint ventures is established by a joint operating agreement. Such agreements are particularly common in North Sea operations since production licences are rarely applied in any way other than through Joint Venture Associations, principally for reasons of cost. The purpose of such agreements is to establish a contractual framework within which the joint venture operations will be conducted by the parties: especially, the manner in which the joint operations will be carried out, and the proportions in which

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1. NISC Report, pp.20-1, Q.3.
2. Proceedings, Vol.I, Paper 14.2. A rather confused treatment of the joint operating agreement can be found in the NISC Report, loc.cit., and also at p.405, Q.204-6: it is not clear what the difference is between a partnership and a joint venture in this account.



costs incurred are to be allocated, as well as the proportions in which any petroleum extracted will be shared out between the joint ventures. Each joint venture is governed by a specific 'operating agreement' which constitutes a common law contract.<sup>1</sup>

This organisational form for individual enterprises has implications for the ownership of oil. To start with, the oil or gas becomes the property of the licensees at the point at which it comes out of the ground: prior to that it remains the property of the Crown. The product at the well-head constitutes the fruits of the 'partnership'. However, ownership of the oil at the well-head is 'divided' according to the party's interest, as is the responsibility to dispose of and transport it. The agreement imposes upon each party a specific duty to take and separately dispose of its oil. Failure to do this constitutes a breach of the agreement.

This has the effect of avoiding any concept of a partnership and of avoiding

... any confusion with American anti-trust legislation when you are involved with US partners.<sup>2</sup>

The terms of each joint venture are such that actual physical ownership of the relevant proportion of well-head output rests in each partner which he may dispose of at will.

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1. A good account of joint operating agreements, and especially of their principal clauses, is contained in Proceedings, vol.I, Paper 14: 'Joint Operating Agreements', by Adrian D.G. Hill.
2. NISC Report, p.42, Q.179. See also T.C.Daintith, Correlative Rights in Oil Reservoirs on the United Kingdom Continental Shelf, op.cit.

The terms of the consortium agreements are regulated solely by operating agreements which are common law contracts, and are subject to the relevant jurisdiction with the UK.<sup>1</sup> Although the detailed terms of these agreements vary from case to case, they tend to function in the following manner.<sup>2</sup>

One of the parties in the venture is selected to act as Operator. As such, he has two separate and distinct roles in the Joint Venture. In the first case, he is co-equal with the other parties, deciding jointly with them what is to be done, and abiding by the agreed decision-making process. All material decisions are discussed in the operating committees on which each partner has a representative although the voting procedure ensures that those parties with the largest financial commitment have the largest number of votes. The results of exploratory surveys are reviewed and drilling programmes discussed. In the second case, as Operator, he is in effect a contractor charged with the task of carrying out what has been agreed and reporting back with the results when it has been accomplished.

The Operator is not therefore the sole party with 'control'. Nor is it the case that the operating committee and other members of the consortium merely play a passive role. Power is not distributed in a straightforward manner among parties to a licence, and when considering the effects of forms of state participation, we

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1. Examples of such agreements are contained in Appendices 3 and 5 (Annexes 1 and 2) of the NISC Report. See also Proceedings, vol.I, Paper 14.
  2. The following is based on an account contained in the NISC Report, Appendix 21, pp.265-6.



must discover how it relates to this process of conducting operations jointly.

In this case, the form of state participation through the nationalised industries did not limit the private appropriation of oil at all. The NCB and the BGC simply participated in joint ventures for the purpose of applying for licences, and then contracted with the oil companies to pay an agreed proportion of the initial and subsequent fees, and any royalties. They met the stated proportion of exploration and development costs and were therefore entitled to an agreed proportion of the oil and gas produced. Representation on the operating committee followed and also the ability to participate in the decision-making process. Profits and losses were shared in the agreed proportion. The details of such agreements were set out in the operating agreements between the parties. Naturally, both organisations built up a staff capacity to deal with the additional work.<sup>1</sup>

To put it bluntly, participation by the nationalised industries in oil exploration required them to adopt a role differing in no significant way from that of a private company participating in a joint venture. Indeed, their participation proved an advantage to foreign companies when applying for licence blocks since it increased their 'weighting' in the discretionary allocation process. For American companies like Gulf and Conoco which had been

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1. This was of course on a much smaller scale than the staff required by the ENOC. The reason being that 'the detailed work that demands large numbers (i.e. of staff) is the responsibility of the operator, and the members of the joint venture pay for this work to be done for them'; NISC Report, Appendix 21, p.266.

slow to involve themselves in the North Sea, state participation of this kind offered a means by which their initial coolness toward North Sea potential could be remedied.

This attempt to 'redefine' public ownership by introducing state participation brought few gains to the Government. 'Participation' only meant a share in licence operations and that on condition the state company behaved like any private company in such circumstances. Such a form of participation was quite compatible with continued private control over licence operations.

However, the idea of state participation had a significance at this time beyond the activities of the National Coal Board, and the British Gas Council. The reasons why participation assumed the form it did reveal much about the relationship between oil companies and British Governments.

A significant attempt to regulate licence operations in the North Sea centred on the state petroleum company proposed by the Labour Party. Obviously, any such proposal raises two spectres for private companies: firstly, the possibility of intervention in private production to the detriment of profitability; and secondly, the probability of competition from an organisation not subject to the laws of the market.

From the mid-1960s onwards, the actions of the Norwegian Government showed that state ownership of oil resources did not necessarily imply a passive role for the state in their development.<sup>1</sup> In addition, the discovery of substantial quantities of natural gas

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1. State participation of some kind (to be arranged by the parties) was made compulsory in Norway in 1967.



in the North Sea led to some demands for greater 'public control'.

In 1967, the Labour Party National Executive Committee recommended that a National Hydrocarbons Corporation be established, following the Report of a Labour Party Study Group on the North Sea. The new institution would have several functions. All unlicensed blocks were to be vested in it and it would take over existing rights of the nationalised industries: the Gas Council and National Coal Board, to participate in onshore and continental shelf operations. In addition, it would have

... the power to search for and produce oil and gas in the North Sea; act as the monopoly buyer of all gas produced by the existing consortia; and be responsible for assessing the economic advantages of the various possible uses and the sale or export of the gas.<sup>1</sup>

Another nationalised industry would thus have been created, but not involving any taking of private rights. Nationalisation of oil companies' operations was excluded.

A similar rejection of nationalisation as 'both impracticable and unnecessary' had been made by one of the Study Group's members, Peter Odell, in 1965. Writing on the subject of 'control' of the oil industry in Britain, he favoured instead 'state co-operation with, and direction of, the oil companies concerned'.<sup>2</sup>

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1. A National Hydrocarbons Corporation, p.2.

2. P. Odell, Oil: The New Commanding Height, December, 1965, p.18.

The proposal for a National Hydrocarbons Corporation was much discussed and elaborated a year later in a report made by the Fuel Study Group established by the Labour Party National Executive Committee.<sup>1</sup> Surprisingly, it was not even partially realised in Government policy in the form envisaged in the plan.

Prior to the third round of licensing, in 1969, the Government instituted a major review of future licensing policy. The review committee included officials drawn from the Departments concerned and also 'top-ranking professionals'.<sup>2</sup> They looked closely at the question of state participation and the idea of a National Hydrocarbons Corporation. Yet in spite of the maturity of the proposal, the presence of a Labour Government, and the innovations then being introduced by the Norwegian Government in its oil policy, it was decided that British oil policy should continue as before with only minor modifications. The basic policy decisions remained the same, as if the discussion of state participation had not taken place at all.

Why was the Labour Party proposal rejected by the Government? As we have seen, this was neither an immature nor a revolutionary proposal. Nonetheless, it was rejected and state participation was only made compulsory in the Irish Sea in the third round. The Department decided that:

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1. A National Hydrocarbons Corporation, p.5 et seq.  
This proposal is also discussed in Adelman's book, op.cit. at p.241.
2. PAC Report, p.27.



... the public interest would best be served by building on the existing arrangements for public enterprise participation in continental shelf activities.<sup>1</sup>

The justification for this decision was extremely weak.

It was argued that expectations at that time were that offshore petroleum discoveries would take the form of natural gas. Since restrictions on the disposal of gas were considered adequate, there seemed no reason for a radical change.

The real reasons can however be located not here nor in any weaknesses of the proposal itself, but rather in the international implications of the adoption of such a proposal.

Right from the beginning of North Sea oil development, British oil policy had been framed with one eye on the possible international ramifications of decisions taken. For example, the financial terms of licences were cautiously formulated because the Department thought that

(i) if the UK were to impose onerous financial terms it might have incited OPEC countries to follow suit, to the detriment of our overseas oil interests and our balance of payments.<sup>2</sup>

Further, in conducting a review of existing financial 'packages' in 1964 (that is, compositions of royalties, annual increments, and so on, to be paid by the oil companies), the Ministry of Power concluded that no existing package was

... ideally suited to the unique circumstances of the UK which had a large stake in the international oil industry, had virtually no indigenous production, but had prospects based on an unproven offshore area.<sup>3</sup>

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1. PAC Report, p.28.
2. PAC Report, p.24, para. 6(iii).
3. op.cit., p.25, para.9.

The 'package' finally agreed upon was

... thought to be as favourable to the Government as any in completely unproved areas throughout the world, while not providing ammunition to OPEC in their demands for higher revenues from British oil companies operating there.<sup>1</sup>

A basic policy consideration was therefore that the terms adopted by the UK should not react unfavourably upon British oil companies operating overseas. While the consideration was probably more important in the first two rounds than in the third, it did not ~~disappear~~ altogether. It appears to have been a dominant assumption that were the British Government to adopt an aggressive stance vis-à-vis those oil companies in the North Sea, this would have constituted a potential danger to the overseas interests of British oil companies.

We can be more precise about the form this question of foreign policy took by the late 1960s. At that time, the British Petroleum Company was attempting to break into the American market through a bid for the Sohio company, as well as its exploration in Alaska and arrangements with two American oil companies, Atlantic Richfield and Sinclair. As one writer has noted:

During 1969 there was real doubt as to whether the American authorities would use the anti-trust regulations to block BP's attempted entry, and, during this period, no British Government was ~~going~~<sup>2</sup> to take actions which might offend the American majors.

It is in this context of international business interests that the real reasons for rejecting the NHC idea can be found.<sup>3</sup> The

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1. loc.cit.

2. L. Turner, in Saeter and Smart, op.cit., pp.97-8.

3. Of course, the Ministers themselves may have disliked this form of state participation on principle. For example, the Minister of Power until mid-1968, Richard Marsh, was described as 'less than lukewarm toward takeover proposals' in The Petroleum Times, September 13, 1978. Cf. Lord Balogh's sharp criticism of Marsh in 346 H.L. Deb. (November 21, 1973) at col.1059.



objections made by the major oil companies themselves to the Government against a State oil company must have carried a great deal of weight in such a context.

While, in practical terms, the idea proved irrelevant, its rejection by the then Government does show how influential foreign policy considerations have been (and can be) in determining the exercise of public ownership of North Sea oil. In addition it provides some perspective for other forms of State participation which have been developed in the UK sector of the North Sea, particularly the British National Oil Corporation introduced much later in 1975.

Another aspect of Government policy at that time was the securing of the maximum share of rent. It is one which need not concern us for long here. The royalties (12 $\frac{1}{2}$ %) were not designed to secure a large share of this, and taxation was not likely to produce a large share. During this period, the objective of securing rent took second place to the two other objectives: promoting the interests of specifically British companies, and securing an intensive exploration programme. This can be seen in various remarks made in the course of the Public Accounts Committee's investigations. For example, the British Government drew on the experience of other countries when working out the conditions to be used in determining the amount of revenue to be derived from North Sea activities. However, one of the three basic policy considerations was that the licence terms should not react unfavourably on the British oil industry operating overseas (i.e. BP and Shell).<sup>1</sup> Hence

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1. PAC Report, pp.24-5, paras.6, 7 and 9.

no existing package of terms used by other countries was thought suitable to the unique circumstances of the UK with a stake in the international oil industry.<sup>1</sup> This keen concern for British oil interests' overseas security and its influence on North Sea policy formation was criticised by the Public Accounts Committee in its report.<sup>2</sup>

To sum up: the licensee certainly obtained a considerable freedom during this period by virtue of holding a petroleum licence. One can legitimately describe this as a kind of 'ownership', although in law there are qualifications to that 'ownership' and it may not even deserve to be designated 'qualified ownership'. However, the manner in which a licensee chose to conduct his operations was left to him, and the obligations contained in the model clauses of licences were few and not onerous. Ministerial powers over licence operations did not include, for example, a power to control the rate at which petroleum was produced. At no time was the degree of state regulation comparable to that present from 1975 onward, whether one considers licensing or state participation.

Governments assumed responsibility for protecting the interests of British oil companies operating abroad, and this 'imperial' role had an influence on domestic oil policy. For example, it inhibited the growth of a state oil company. By contrast, the Norwegian Government had a greater flexibility in its oil policy, since it had no historical or structural links with the large oil companies.

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1. op.cit., p.25, para.9.

2. op.cit., pp.xxv-xxvi, para.73.



#### 4. The Crisis of Legality

Until 1974, the system of licensing blocks on generous terms proved highly advantageous to licensee companies. The rights which successive Governments transferred allowed the companies a degree of economic control over exploration and production which, in the event of success, guaranteed a very high rate of profit on oil: so high, it was exceptional in Britain, and compared favourably with that obtaining on investment in South Africa. As one firm of stockbrokers, Cazenove and Co., pointed out:

Irrespective of accuracy, it is apparent that the return from North Sea oil will be considerably more than the international majors are currently obtaining from their<sup>1</sup> heavily taxed Middle Eastern and North African sources.

The regulatory controls contained in the model clauses of licences did not reduce the companies' control over their operations in any significant way. In addition, no threat was posed by the form of state participation which operated in the North Sea: compared with forms of participation favoured by OPEC members, it imposed little additional burden, if any, upon oil companies.

However, these conditions had begun to change after the fourth round of licensing in 1971-2. The allocation of a large number of licences on terms which remained substantially unchanged from those awarded in 1964, in spite of the fact that recent

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1. Cazenove and Co., The North Sea: the search for oil and gas and the implications for investment, 1972, p.113.

discoveries clearly showed the potential of the northern North Sea, began a controversy which was ultimately to lead to a revision of the licence terms in 1975.

In retrospect, it is not difficult to see why the fourth round proved so controversial. To begin with it was very large, although not the largest: 282 blocks were awarded covering 24,000 square miles, compared with 348 blocks covering 32,000 square miles in the first round, and 127 and 106 blocks in the second and third rounds respectively.<sup>1</sup> As an experiment in a different mode of allocation, 15 blocks were allocated by auction. The sum of the highest premium bids for each of the 15 blocks put out to tender totalled £37 million,<sup>2</sup> a fact known to the Government before the 282 blocks were allocated on a discretionary basis. It was, therefore, known to the Department of Trade and Industry how highly the applicants valued some of the territory before the larger number of blocks were allocated by discretion. Nonetheless, the results of the auction did not, in their view 'invalidate the policy reasons which led Ministers to their original decision to proceed with a round of discretionary licensing simultaneously with the tender experiment'.<sup>3</sup> Since the terms of the whole offer had been publicly announced and applications submitted on the basis of those terms, it was thought that setting the terms aside in the light of the auction experiment's results 'would have been criticised as a serious breach

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1. PAC Report, p.45.

2. op.cit., p.33, para.48.

3. loc.cit. p.33, para.48.



of faith on the part of the Government and would have jeopardised Her Majesty's Government's reputation for fair dealing'.<sup>1</sup>

This emphasis upon rectitude might have seemed more plausible had the licence terms not been identical to those in earlier rounds; even those of the first round in 1964 when applicants considered prospects good only for gas! Licences were still being granted for an initial period of six years, and half this area could be held for a further forty years. There was no provision for re-negotiation of the terms. Yet circumstances had altered dramatically since the early rounds: as early as June, 1970, a consortium including Phillips, BP and Shell, discovered oil in the northern North Sea in territory licensed in the second and third rounds. An earlier discovery, Ekofisk, on the Norwegian side of the median line was estimated by mid-1970 to have a production potential of 150,000 barrels a day.<sup>2</sup> Between the end of October, 1970 and June, 1971, several discoveries were made and were declared commercial: the Forties Field, held to be in the world class, and Auk, Josephine and Brent.<sup>3</sup> The prospects for discoveries of oil in large quantities in the North Sea were good.

Yet in spite of this radical change in prospects, a large number of licences were awarded on terms identical to those awarded at the time of the first round in 1964 when virtually nothing was known about prospects for oil and gas in the North Sea. The official justification for this was based on the need to halt a reduction in

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1. loc.cit.

2. PAC Report, p.30, para.34.

3. This latter discovery was not however made public knowledge until 1972.

drilling activity on the continental shelf which was causing some concern. The number of exploration wells drilled in 1969-70 was 47, while the number in 1970-71 was only 22. As the number of obligatory wells remaining to be drilled under earlier work programmes had fallen to below 50, a smaller number of rigs would be needed in future. It was concluded that a major licensing round was required to open up further territory for exploration, and

to attract to the United Kingdom shelf more of the technical and financial resources of existing operators as well as those of companies not so far represented.

Otherwise these resources might go elsewhere.<sup>1</sup> When measured against work to be undertaken in exploring blocks, the round was highly successful. Two hundred and twenty-five wells were to be drilled according to the work programme. This emphasis upon a work programme followed the pattern established by earlier rounds in which the licence conditions were geared to rapid exploration for oil and gas, and gave little weight to revenue.

However, another explanation is more plausible. The then Government was for the most part ignorant of the resource potential in the British sector of the North Sea. A detailed assessment of 'oil traps' could only be built up as wells were drilled and the extensive seismic information evaluated. While the oil companies certainly submitted much information concerning seismic and drilling

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1. PAC Report, pp.30-1, para.35. It was also argued that the balance of payments impact of recent OPEC actions made intensive exploration and development more pressing than ever; also that since a number of part-blocks had been surrendered it made sense to make them available for further exploration at once rather than to let them lie.



results (as they were required to do), the technical competence of the Ministry was poor: the technical staff numbered six in 1970 and seven in 1971. This lack of technical expertise may go some way to explaining why the Department was still in doubt whether a major oil-bearing province had been discovered or not.

As a way of obtaining knowledge of the blocks' market value, a small auction experiment was perfectly appropriate in the circumstances. However, by holding it simultaneously with a large discretionary allocation, there was no opportunity to learn from the experiment until after the round; that is, until after a large number of licences were allocated on terms which envisaged no amendment at a later date. There was then a greater body of information available about potential oil reserves than was subsequently claimed and more information was obtained after the auction experiment. Whatever uncertainty remained about potential reserves in the North Sea, it cannot be seriously contended that oil discoveries on a large scale were not expected at this stage.

Much of the criticism directed at this round was highly partisan politically, aimed either at the Department of Trade and Industry, or more broadly, at the Conservative Government. While this is hardly surprising given the consequences of policy decisions in the fourth round, it is possible that a false perspective might be created, suggesting that the oil companies' unusually advantageous position was entirely the result of a Conservative

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Government's policies. In fact, the round was very like previous rounds and the policy considerations differed little from those of successive Governments since 1964. One might note that the Labour Governments from 1964 to 1970 did nothing to modify licence terms, in spite of some criticism of the first round awards while in opposition. In those six years, the Labour Governments made no significant innovations in licensing policy, apart from putting some stress on participation by the nationalised industries.

Nor should the novelty of an auction experiment be misunderstood. The auction method of allocation was considered in the review which preceded each round. An auction experiment seems to have been considered at the time of the third round.<sup>1</sup> An auction experiment would have provided a useful indication of the value of blocks at an important stage in North Sea development. The new developments in rig technology allowed exploration in the deeper waters of the northern North Sea and it was likely that blocks in that area would be in demand in the near future: hence, the suggestion of a small auction experiment which could have produced information useful in future allocations. The imminence of a General Election may have persuaded the Government that such a consideration was not of the greatest importance.

Finally, the blocks allocated in the fourth round were not necessarily the most productive ones: quantity is not the same as quality. Although fewer blocks were allocated in the third round, for example, their oil-bearing potential was considerable. Of the 9 billion barrels of recoverable reserves being produced in 1978

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1. PAC Report, pp.28-9, paras. 24-5. Interview with Angus Beckett Under Secretary at the Ministry of Power and Technology, 1969-70.



or planned for production, about half had been found on blocks awarded in the third round.<sup>1</sup>

The inquiry conducted by the House of Commons Public Accounts Committee into the arrangements for exploiting North Sea oil and gas did nothing to soothe any anxieties which might have been felt after the fourth round. Its report, published in early 1973, was highly critical of government policy and of the existing licensing and taxation arrangements.<sup>2</sup> Moreover, the fact that the Committee was composed of MPs from both the major political parties and had a Conservative majority gave its report added force.

The principal points of criticism concerned, firstly, the terms on which licences were allocated. In the light of the improving prospects of the North Sea and the hardening of terms in other countries, the Government should have considered tougher terms.<sup>3</sup> Too many licences had been allocated for the most promising areas of the North Sea. Moreover, they had been awarded on terms which had remained virtually unchanged since they were fixed in 1964.<sup>4</sup> Those terms allowed licences to run for forty-six years in respect of half the territory.

Secondly, it criticised the taxation arrangements.<sup>5</sup> Since taxation was the principal method by which the Government could obtain rent from the oil companies, it was of considerable

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1. A. Hamilton, North Sea Impact, p.108, note.

2. PAC Report, op.cit. The Committee took care to emphasise that they were not criticising the part played by the licensees in exploring for and exploiting oil and gas: see para.53.

3. PAC Report, para.86.

4. op.cit., para.88.

5. op.cit., paras. 62, 66, 97(1) and 97(2).

importance. In this respect oil differed from gas: since the pricing mechanism of oil was beyond Government control, it was not able to take a share of ~~company~~ profits by keeping them low, as it could do with gas.

However, there was a loophole in the taxation system which allowed oil companies to pay only minimal taxation. Under the then UK tax law, companies would be able to write off against eventual North Sea profits not only the capital allowances engendered by these operations, but also massive tax losses accumulated by the trading companies of large integrated oil companies abroad, principally as a result of the posted price system operated by the OPEC countries. That is, UK tax revenues from continental shelf operations were being pre-empted by other national Governments.

The Committee was careful to emphasise that while this would benefit the oil companies, not all the companies operating offshore were in fact oil companies: about one half of the 240 companies which held production licences for the continental shelf were not oil companies, e.g. ICI.<sup>1</sup>

It recommended that a change be made in the taxation arrangements, and that a review of the licensing regime be conducted in the light of the Report in order to increase the Government's share of rent.

A climate of dissatisfaction with the existing relationship between the State and the licensee companies in the North Sea was

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1. op.cit., para.54 (p.XX).



developing in 1973. The knowledge that the economic benefits from the recently discovered oilfields would accrue to the licensees alone, and to the oil companies in particular, provoked demands for political action.<sup>1</sup>

However, the principal factor which rendered the existing licensing and taxation arrangements intolerable was the 'oil crisis' of 1973-4, and specifically the quadrupling of oil prices in a few months. From this followed a massive increase in the profitability of North Sea oilfields, and in the overall profits of oil companies. Since the British Government could not claim any significant portion of the new profits to be made in the North Sea on the basis of the existing arrangements, the generosity of those arrangements was merely underlined. This also applied to those marginal fields that were suddenly made 'economic' by the price rise: that is, the fields which had their development cost reduced relative to the future profits on oil extracted and sold.

In addition, the strategic importance of oil for the advanced capitalist societies was underlined. Each state saw its control over oil supplies threatened and began a review of its oil policy. Those states fortunate enough to have indigenous supplies of oil obviously

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1. For example, Labour's Programme 1973, p.32, and the various speeches made by Lord Balogh: e.g. 336 H.L. Deb. (November 22, 1972) cols. 996-1005; 337 H.L. Deb. (December 13, 1972) cols. 662-666; 331 H.L. Deb. (June 7, 1972) cols. 362-403; 346 H.L. Deb. (November 21, 1973) cols. 1057-1068. See also his article, The North Sea Oil Blunder, in The Banker, March 1974, at p.287: 'I think this revolution (i.e. the OPEC price rise and oil embargo) amply justifies the need for re-negotiation'.

had fewer problems in this respect. Yet, in spite of the discovery of large quantities of oil offshore, the British Government had virtually no regulatory controls over oil supply. Acquisition of emergency powers seemed a matter of priority.

For a number of reasons then, the existing licence and taxation arrangements between oil companies and the British State were no longer perceived as legitimate by early 1974. The Conservative Government had itself acknowledged this by instituting a review of policy and announcing its intention of modifying the taxation arrangements to close the 'loopholes' discovered by the Public Accounts Committee. Whatever the views of the oil companies, large numbers of people did not regard these arrangements as fair and legitimate. This was compounded by a general economic and political crisis: a powerful current of nationalism in Scotland was accompanied by severe industrial strife in Britain as a whole, and the first major economic recession since the 1930s began in Autumn 1973.

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**CHAPTER THREE****The Revision of Licence Terms, 1974-5**

No other European nation has proposed to subject its offshore operators to retrospective legislation on existing licences.

Vice-President, Amoco Europe<sup>1</sup>

To raise the idea that this is a violation of property rights, which is the sort of behaviour of a banana republic after a Trotskyist take-over, is to do less than justice to the gravity of the Government of the day.

Tony Benn, Energy Secretary<sup>2</sup>

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1. Steve Antoniuk, Vice-President of exploration and production, in The Scotsman, 'US Oilman condemns "breach of contract"', May 16, 1975.
  2. Petroleum and Submarine Pipe-Lines Bill, H.C. Deb. Standing Committee D, col.1164 (July 3, 1975).



Contents:

1. The controversy
2. The role of negotiations in developing the new framework
3. The debate in Parliament
  - (i) the power to control the rate of production
  - (ii) other regulatory powers
4. The meaning of 'unilateral'

I have dwelled at some length on developments which occurred during North Sea oil's 'pre-history', since they underline the scale of the problem which faced the Labour Government in 1974. The state's involvement in North Sea oil developments had been limited to actions which assisted the oil companies, and especially British ones, in whatever way possible. For a period of more than ten years holders of petroleum production licences in the UK were entitled to conduct their exploration and exploitation subject to minimal regulatory constraints: the best part of a licence could be held for up to forty-six years; there was no limit on the rate at which oil was to be extracted once discovered nor on the manner of extraction; the licensee had an exclusive right to all the oil once it was extracted; there was no provision for re-negotiation of licence terms once the licenses were allocated; the quantity of information the licensee was obliged to disclose was small; if oil resources were found, it was up to the private oil companies to decide whether or not to develop a particular field; and tax avoidance on a large scale was not especially difficult under the existing legislation. During this period licences were allocated in four rounds for a very large number of blocks which by 1974 were known to contain most of the recoverable reserves of oil in the North Sea. Any effective increase in state involvement in North Sea oil development and production had to be directed at the terms of existing (i.e. pre-1974) licences.

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The manner in which the new Labour Government planned to secure effective control over oil resources in 1974 created a crisis of legality. The introduction of new regulations into the model clauses of existing production licences was to be achieved unilaterally. While there was no legal barrier to this action by the state, it raised a broader question about the legal security of any private interest or interests vis-à-vis the state. After all, these licences not only contained regulatory elements in their model clauses, but also had a contractual character. Since the effect of this action would be to render the licence less valuable to the licensee, it also seemed like a form of expropriation. The Government vigorously and repeatedly denied that this was the case not only because it implied that payment of compensation should accompany the legislative action, but also because, if correct, the British Government appeared to have qualified its respect for the principles of the Rule of Law and *pacta sunt servanda*. In order to respond to the latter, and ultimately more serious implication of its sovereign action, the Government strove to find a legal form which reconciled its legislative intent with an attitude of respect for the legal principles. In this chapter I explain how the Government achieved this, and why it mattered so much.

#### 1. The Controversy

However favourable licence rights were for their recipients in the first four rounds, they seemed threatened by the state

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intervention proposed by the Labour Government in 1974.

The Labour Party's Election Manifesto for February 1974 had originally set out two principal objectives for a Labour Government with respect to North Sea oil. Firstly, the character of this natural resource as a publicly-owned resource had to be ensured, and secondly, 'the operation of getting and distributing them' had to be placed 'under full Governmental control with majority public participation'.<sup>1</sup> It was claimed that public ownership and control was essential to allow 'the British people, through its Government, to fix the pace of exploitation of our oil, and the use to which it is put'. This implied a considerable reduction of the role of private enterprise in oil production, and also a reduction in the profitability of oilfields. Both these objectives were to be vigorously opposed by companies whose initial interest in, and commitment to, North Sea exploration had been quickened by the prospect of high profits once oil was discovered in large quantities.

After considering the matter for four months, the new Labour Government produced a White Paper in July 1974, in which it put the objective of securing 'effective control' over the oil reserves alongside another principal objective: that of increasing its share of rent.<sup>2</sup> By this it meant that the balance between profits accruing to the oil companies and revenues to the state was

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1. All references in this paragraph are to the Election Manifesto, February 1974, p.3.

2. Department of Energy, United Kingdom Offshore Oil and Gas Policy. Cmd.5696 (1974) (Hereinafter 'White Paper'): the relevant passages are on pp.4-6.



to be redressed, as well as maximising the balance of payments advantages by reducing remittances of profits to foreign parent companies. The 'control' objective was to be achieved by two methods: firstly, new regulations were to be introduced into the model clauses of existing and future petroleum production licences; and secondly, majority state participation would be introduced in all oilfields declared 'commercial'. In November it was announced that the legislative instrument for achieving this (non-fiscal) objective was to be the Petroleum and Submarine Pipe-Lines Bill (and specifically Parts I and II of that Bill),<sup>1</sup> supplemented by 'voluntary' negotiations on participation (discussed in the next chapter).

The anxiety felt by the Government over the legality (and the economic ramifications) of its decision to unilaterally revise the terms of existing (as distinct from future) licences led it to issue an invitation in the White Paper to the oil companies

... to join in working out a new structure which they know will be durable<sup>2</sup> because it will be accepted by the people of Britain.

These negotiations were to be an important means of securing the companies' consent to a new legal framework for oil licensing, as well as a means of working out the details of such a framework. However, the very explicit use of negotiations was also an attempt

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1. See The Financial Times, 'Final Clarion Calls to Battle', November 15, 1974; by contrast, the licensees had known details of the proposed Petroleum Revenue Tax for several months.
2. White Paper, p.9.

to deal with a persistent problem in oil company-state relations in the UK, deriving from the fact that the state has two sometimes contradictory roles: on the one hand, it is the licensing authority, concerned to regulate licensees' activities, and on the other, it is a party to a contractual arrangement. This dual role of the state is reflected in the licences themselves which have both regulatory and contractual elements. It has not always been easy to distinguish the two, nor to ascertain which predominates. The use of negotiations helped cast the state in the role of a 'party' to a bargaining or exchange relationship, thus mollifying somewhat the use of political power. Nonetheless, the bargaining only began as a result of the state's unilateral decision to invalidate the original grant of a licence!

However, there was no real alternative to this exercise of sovereign power if the Government was to achieve its objective of 'public control'. By 1974, North Sea oil development had reached a turning point. Those oilfields which were the largest and easiest of access had been discovered under licences already awarded. Consequently, any changes in licence terms had to be directed at existing licences rather than future ones if they were to have any practical effect in the near future. Such changes would have an immensely greater economic significance than would the imposition of additional obligations on applicants for licences in future rounds. While changing the terms of future

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licences posed few legal problems if any (since new regulations could be made under the Petroleum (Production) Act 1934, with new model clauses to be included in those licences), changing the terms of existing licences posed several.

The Government probably considered three modes of procedure:

(1) it could have tried to secure the consent of all existing licensees to the alteration of their licences in the required manner. Given the diversity of interests and circumstances among the licensees this was impossible to do consistently, and would probably have involved some large financial cost to the state: a most unattractive feature so far as the Government was concerned. In addition, the amendments which the Government had indicated it wished to make would have given it new powers the use of which might impose substantial new costs on the licensees and diminish profits (e.g. the proposed powers to impose bigger development programmes, to restrict rates of depletion, and to take royalty in kind<sup>1</sup>): licensees were unlikely to agree to this. Finally, many of the existing licences had many years still to run and were therefore of considerable value to a licence-holder. In the case of those awarded in the fourth round, they had more than forty years to run: why should such licensees surrender any of their material advantages?

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1. Principally, Model Clauses 15, 16 and 11.

(2) it could have secured the enactment of legislation imposing new obligations (over depletion control, for example) outside the framework of the licences as a matter of unilateral regulation. The difficulty with this course was that it might create risks of conflict between the contractual obligations imposed by the licence and those imposed by external regulation. In its favour it would have kept separate the state's two roles of contractual party and sovereign power.

(3) it could have secured the enactment of legislation effecting or empowering the unilateral alteration of the (contractual) licence terms themselves. Since there are no formal limits on Parliament's legislative competence in the UK, this course was perfectly feasible and, indeed, was the one chosen by the Government: it obtained legislative authority for the substitution of new terms in existing licences. It also took the step of incorporating all the clauses for substitution in existing licences in the same Bill which conferred authority for the unilateral action, rather than simply seeking the enactment of a general empowering provision. The salient point about such a course is that it enabled the new clauses to be discussed in considerable detail (and substantially amended in Parliament). It also provided a framework which encouraged the oil companies to make specific their objections to the Government's proposed changes in the regulations, especially those governing development and production.

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The most controversial provision was contained in clause 18 of the Bill, and concerned the modification of model clauses which were standard form for all petroleum production licences in the UK. Its objective was to alter the terms of existing seaward and landward petroleum production licences (i.e. those awarded in the first four rounds) by substituting the clauses contained in Part II of Schedule 2 and 3 contained in the Bill for clauses originally contained in the licences. As Daintith and Willoughby point out, this is an unusual provision.<sup>1</sup> While Parliament frequently enacts legislation which makes the performance of particular contracts financially less attractive for the parties, and while it is not unusual for it to enact legislation which is incompatible with existing contracts and therefore demands their amendment (for example, the Resale Prices Act 1964, and the Sex Discrimination Act, s.77), or even to enact legislation which authorises departures from such contracts for the purpose of promoting government policy,<sup>2</sup> they make the claim that

... it is without precedent in the United Kingdom to make a unilateral alteration of the terms of contracts by legislation.<sup>3</sup>

They also emphasise that these changes, which were given effect, were

...not of a purely technical character, but impose substantial new duties on licensees.<sup>4</sup>

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1. Manual, pp.305-6.

2. They cite s.1 of the Remuneration, Charges and Grants Act 1975 as an example.

3. Manual, p.306.

4. loc.cit.

Not surprisingly, the retrospective character of clause 18 made it an object of criticism by the Opposition at every stage of the Bill's passage through Parliament.<sup>1</sup> In defence of the Government's action, Lord Balogh, the Minister of State for Energy, explained that although it was 'regrettable' that powers had to be taken unilaterally to alter the terms of existing licences, this was merely a consequence of the 'unfortunate but manifest inadequacy of the existing terms'. The Government's action was

... not retrospective but remedial action in the national interest to eliminate certain weaknesses in the licensing system.<sup>2</sup>

This was not an example of retrospective legislation in the commonly accepted sense, and the Minister of State at the Scottish Office, Lord Hughes, added that

... nothing in the Bill makes anything illegal which at the time it was done was legal.<sup>3</sup>

While the new regulations certainly did apply to existing licences, this was 'only in respect of future actions carried out under them'. There was therefore no question of compensation.

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1. 891 H.C. Deb. cols.503-6 (April 30, 1975); H.C. Deb. Standing Committee D, cols.1105-72 (July 3, 1975); 896 H.C. Deb. cols. 1436-46 (July 28, 1975); 363 H.L. Deb. cols.1955-6 (August 7, 1975); 364 H.L. Deb. cols.546-74 (September 25, 1975); 899 H.C. Deb. cols.465-82 (November 3, 1975); 365 H.C. Deb. cols. 1764-8 (November 11, 1975). For one instance of possible retrospective effect of ss.18 and 19 of the Act, in spite of s.19(3) which provided that acts or omissions occurring before a licence was altered are not to be treated as contravening the provisions of the altered licence, see Manual, p.474 (note to Petroleum (Production) Regulations 1976, Schedule 5, cl. 40(4)).
  2. 365 H.L. Deb. col.1768 (November 11, 1975). See also remarks by Edmund Dell in the proceedings of the Financial Times Scandinavian and North Sea Conference, held at Oslo, September 1, 1975.
  3. 363 H.L. Deb. col.404 (July 23, 1975). The following quotation comes from the same place.



However, another Minister, Mr. John Smith, was reported to have said that the legislation 'could enable retrospective controls to be introduced'. In his view this was justified since otherwise the best parts of licences awarded in 1971 would run until 2018 without the Government having control over rates of production.<sup>1</sup>

In other words, this was retrospective legislation in a sense but not in a commonly accepted sense!

Against this, the Opposition argued that a unilateral alteration of a contractual licence which rendered the licence less valuable constituted a form of expropriation of property without compensation. As such it was contrary to international law and certainly marked a diminution in the respect paid by UK governments to the principles of the Rule of Law and the sanctity of contract. This argument was rejected by the Government, on the ground that the legislative change was being brought about

... on the basis of good faith and good working relations with the oil companies ... as anyone dealing with any British Government would expect.<sup>2</sup>

Undeterred, and in pursuit of their conception of legality (as well as the oil companies' interests), the Opposition tabled an amendment which would have provided compensation where a licence was revoked for non-compliance with a provision unilaterally inserted

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1. 'Oil search could now move to Moray Firth' in The Scotsman, May 20, 1975. In Committee, he said: 'Of course the changes are retrospective. I have never made any attempt to deny that. However, I believe that they are absolutely necessary'. (H.C. Standing Committee D, col.1114, July 3, 1975).
2. 899 H.C. Deb. cols.467-8 (November 5, 1975).

in it by reason of the Act. This was however defeated by the Government.<sup>1</sup>

Of course, payment of compensation was anathema from the Government's point of view, since it would have been on a massive scale and would have supported the Opposition's contention that the provisions of the Bill, and in particular the first part concerning the establishment of a state oil corporation would lead to a massive increase in public expenditure, at a time when it was widely accepted that a general reduction in such expenditure was required.

A further weakness in the compensation proposal was not discussed at the time. Once the Government had announced its intention to change the licence terms unilaterally (in form, at least), the situation of the licensees was changed at a stroke, making it impossible to establish without the greatest difficulty what the value of the licences was. The decision to revise the terms must immediately have altered the value of the existing licences, thus making any determination of the exact loss which a licensee would incur a complex if not impossible matter. This situation differs from that of nationalisation too. Here, the licence is a bundle of contractual rights still of value to the private party after the state acting as public authority takes a course of action which has reduced the original value. It is not possible to assess the value lost as a consequence, and hence

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1. 365 H.L. Deb. cols.1764-8 (November 11, 1975).



bargaining over compensation is rendered difficult, if not impossible. The situation created by a decision to nationalise is, however, quite different: the Government announces its intention to nationalise and at a stroke affects (and probably reduces) the value of the property concerned. Nonetheless, it is clear that everything is involved: the agreement reached and the nationalisation Act is one concerning all the goods and all possibilities of profit.

Superficially there was a parallel between the Government's action and the sorts of action taken by various OPEC states from the early 1970s onward. There too one could find the unilateral aspect as well as demands for sweeping changes in the existing legal arrangements between oil companies and governments. Such a view was encouraged by statements like that of Lord Balogh when he said that

... we must look at the outside world and try to draw <sup>1</sup> lessons from what other major oil producers have done.

However, such parallels neglect the very important fact that the forms of state involved are quite different. Whereas many oil producing states have been concerned to use their resource as part of a broad attempt to throw off a colonial yoke and to industrialise

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1. 363 H.L. Deb. col.329 (July 23, 1975). Nonetheless, he did not approve of the more radical conclusion drawn by some members of the Labour Party, and was suspicious of their use of 'the idea of national oil ownership': see 'The North Sea Oil Blunder' in The Banker, March, 1974, p.288.

their economies, the form of state in Britain is one peculiarly suited to that of an advanced capitalist society which requires a very different role for the state. For example, successive British Governments have always recognised that the British state has a role of caretaker vis-à-vis the extensive British investments in overseas countries and cannot therefore adopt a cavalier approach to the international standards of legality which, if respected, allow that investment a considerable degree of security. Government spokesmen were in fact well aware of this difference.<sup>1</sup> Indeed, it was this very difference which made the unilateral character of the state's action a matter of such concern, and this international range of <sup>interests</sup> concerns which made considerations of international law so important.

There were two ways in which the latter had a particularly important role to play. Firstly, a unilateral change in licence terms which was a clear and unambiguous violation of international law would be likely to produce a political confrontation with the United States, whose companies constituted the majority of foreign companies operating on the UK Continental Shelf. Indeed, the US Treasury registered its opposition to the Labour Government's plans throughout 1974. For example, British parliamentarians who visited the United States in September were warned that the proposed revision of licence terms might encourage American companies

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1. Cf. Lord Balogh's criticism of the Conservative Government's approach in the fourth round of licensing: 'The Government continued to give these rather splendid terms as if we were a banana republic', 365 H.L. Deb. col.1768 (November 11, 1975); see also Benn's remark quoted at the beginning of this chapter.



to withdraw their oil rigs from the North Sea. The House of Commons sub-committee on energy, visiting Washington to examine American energy policy, were told that the US Treasury and the Department of the Interior were studying the possibility of offering US oil companies fiscal incentives to repatriate scarce oil rigs from the North Sea to conduct exploration in American waters.<sup>1</sup> In the event, this proved an empty threat, but it may have lent support to American companies in the subsequent discussions with the Department of Energy in Britain. British MPs were left in no doubt that the US Treasury's attitude had been influenced by the Labour Government's plans, including its intended introduction of majority state participation.

Secondly, international law considerations were important because of the stake which British-based companies and banks had not only in the international oil industry but in the world economy. It was probably thought that the overseas interests of British Petroleum in particular might be rendered less secure if the British Government were to put itself in a position from which it could not assert international law principles against other Governments should they take actions hostile to British interests abroad. The close connection between British

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1. The Financial Times, September 7, 1974: 'US may offer incentives to repatriate North Sea rigs'. However, another reason for the actions of the US Treasury was the so-called Project Independence, under which the Ford Administration committed itself to making the US self-sufficient in energy by 1985. This involved several measures like increasing the programme of exploration and drilling offshore in the US, for which new rigs were required at a time when there was a worldwide shortage.

Petroleum and the British Government made it particularly vulnerable. In 1974 this share had increased to 68% when the Bank of England acquired a share previously held by the Burmah Oil Company. However, many non-oil British companies and banks also have assets and capital investments in other countries. As Mr. Patrick Jenkin pointed out, Britain is a 'major capital exporting country with investments in many countries overseas'.<sup>1</sup> The continuing importance of this factor was underlined in the evidence submitted by the Committee of London Clearing Bankers to the Wilson Committee on the functioning of financial institutions. It said:

A feature of particular importance to international banks has been the increasing volume of capital goods exports, requiring medium and long term financing. UK exports of capital goods rose from 25 per cent of the total (of all exports) in 1959 to more than 42 per cent in 1976, and over this period the sterling value of exports rose roughly eightfold.<sup>2</sup>

From 1960 to 1976 the percentage of UK exports going to OPEC countries rose from 5.9 per cent to 12.2 per cent.<sup>3</sup>

Not surprisingly then, the consequences of the proposed legislation for the security of those overseas investments was a persistent cause for concern, especially in the Conservative Party. When the Bill was going through its Committee stage, it was pointed out that British companies (and not only oil companies) were already

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1. H.C. Deb. Standing Committee D, col.1148 (July 3, 1975).
2. The London Clearing Banks: Evidence by the Committee of London Clearing Bankers to the Committee to Review the Functioning of Financial Institutions, November, 1977, pp.122-3.
3. loc.cit., p.123: Table 21.



involved in disputes over their commercial interests with at least half a dozen foreign countries which had taken action similar to that being proposed by the Labour Government.<sup>1</sup> The British Government - or, more accurately, the British state - was seeking in these disputes to establish compensation for British subjects in respect of property expropriated by foreign governments without adequate compensation. In this context the pre-occupation of some members of both Houses of Parliament with the issue of compensation was an expression of a general concern for the interests of all transnationally operating capital units based in Britain (or 'international capital'), and not merely a concern over adverse affects upon oil companies' interests in the UK (although it was that too).<sup>2</sup>

It was in order to extricate itself from this complex situation that the Government decided on a twofold course of action: the legislation would be designed to facilitate maximum discussion and amendment in detail of the proposed regulations in Parliament; and the oil companies would be invited to 'talks' with the Government in which they could discuss the legislation and suggest amendments to it - in private. This way it was hoped to circumvent the major problems I have outlined above and, in particular, the possibility of economic retaliation.

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1. H.C. Deb. Standing Committee D, cols.1148-9 (July 3, 1975). See also the remarks made by Mr. Blacker at 891 H.C. Deb. cols.565-7 (April 30, 1975). The countries included Libya, where £250 million worth of British assets (estimate) had been expropriated since 1969, and Uganda, where the value of property expropriated was thought to be worth as much as £500 million. The result of the Arbitration between BP and the Libyan Arab Republic is to be found in 1979 ILR at p.297.
2. Frankly admitted by Lord Campbell of Croy at 365 H.L. Deb. col.1766 (November 11, 1975).

## 2. The role of negotiations in developing the new framework

The new legal framework was shaped both by Parliament and by the Government and oil company negotiators. In effect, there were two main sets of discussions over the proposals in the Petroleum and Submarine Pipe-Lines Bill. The first took place in Parliament (itself) between the major political parties, and the second took place outside Parliament, between the Department of Energy and the licensees, represented by the UK Offshore Operators' Association. Of the two it is impossible to state which proved most influential in securing amendments to the legislation since the latter took place in private.<sup>1</sup>

The two sets of discussions were not entirely separate either. There was some interaction between the parliamentary debate and the confidential discussions in the offices of the Department of Energy at Millbank. Possible amendments to the legislation, proposed by either party, were advanced and discussed in the private forum, and then sometimes advanced by the Government itself in the parliamentary forum if agreement had been reached in the private discussions. Indeed, many amendments were proposed by the Government itself.<sup>2</sup> Where the Government would not go so far as to propose or accept an amendment, it sometimes provided assurances about its intentions and its use of the powers it proposed to take.<sup>3</sup>

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1. My own knowledge of these discussions is based principally on the results of a series of interviews I held with participants in these discussions during Spring and early Summer, 1976.
  2. For example, Model Clause 31 (release of data) in response to suggestions by the UKOOA: H.C. Deb. Standing Committee D, cols. 1397-99 (July 8, 1975) and Model Clause 14 (exploration) also in Committee at cols.1237-42 (July 3, 1975); and see s.3 of this chapter.
  3. For example, Lord Balogh gave an assurance about the use of the Government's power to revoke a licence at the Report stage of the Bill: 365 H.L.Deb. cols.580-1 (October 29, 1975).



I shall examine some of the principal aspects of the first set of discussions (in Parliament) in the next section of this chapter, but some general comments on both sets of discussions are in order here.

The oil companies took steps to ensure that Members of Parliament were aware of their objections to the Bill. For example, company advice was freely given: indeed, oil company advisers were present at the Committee stage where so many important amendments were made.<sup>1</sup> In addition, a special committee was established to advise the Conservative Party.<sup>2</sup> The Energy Advisory Committee was set up as a forum in which to discuss and draft amendments initially to the Oil Taxation Bill and later to the Petroleum and Submarine Pipe-Lines Bill. It was designed to assist the Conservative Party in its opposition to the Government's legislation in Parliament. Its members included the Conservative MPs, Trevor Skeet and Patrick Jenkin, the latter being the then 'Shadow' Energy Secretary; and several volunteers from the oil companies, including British Petroleum, Amoco, and Mobil. It held between 3 and 6 meetings over a five-month period. According to one source, the smaller oil companies were particularly active in this forum.<sup>3</sup>

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1. All the persons I interviewed in the oil industry confirmed this.
  2. The following draws on several interviews with company negotiators in the Amoco, Mobil and Gulf companies.
  3. Interview with Mr. D. Vock, senior counsel, Mobil Oil company.

The second set of discussions between the licensees affected by the Government measures and the Department of Energy were 'quite frequent' in the various stages of the Bill's passage.<sup>1</sup> However, they presented special difficulties, since there were many different types of company with interests in pre-1974 petroleum licences,<sup>2</sup> and some means had to be found to centralise the many different responses to the Government proposals. Such a process of centralisation was supported (and encouraged) by the Government itself.<sup>3</sup> As is customary in the international oil industry, it was the Operator in each licence arrangement who was assigned responsibility for the negotiations with the Government.<sup>4</sup> Since most, though not all, Operators were members of the United Kingdom Offshore Operators' Association (hereinafter the UKOOA), the informal talks and consultations were held between the Department and the UKOOA. The latter body had two committees for consultations with the Government, and the relevant one here was the Non-Fiscal Legislation Committee.<sup>5</sup> Not surprisingly, the Licence Operator was always an oil company and, given their considerable interests in the North Sea, the Operator

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1. Interview with Mr. A.R.L. Murray, Department of Energy.
  2. See chapter one for an account of this.
  3. See the comments in The Financial Times, 'Seeking one industry voice on PRT', January 10, 1975.
  4. For an explanation of the Operator and his role in joint venture arrangements, see chapter two, s.3. The key role of North Sea Operators in the negotiations and discussions with the Government at this time was confirmed by the individuals I interviewed.
  5. Interview with Mr. M. Ambrose, and Mr. J. Essex, Amoco Oil Co.



was often one of the major international oil companies or 'the Seven Sisters' as they have been called. Such companies were therefore negotiating with the Labour Government on behalf of <sup>almost</sup> all the companies with interests in existing petroleum production licences.

As we shall see, the lengthy and detailed discussions of the legislative proposals had the effect of ensuring that the revision of licence terms allowed for greater state regulation but without any significant reduction in the future profits of those companies with North Sea investments.

However, any consideration of legal and political structures which omits their interaction with, and ultimately their dependence upon, economic structures must lead to a one-sided view of developments within those structures. Both the formal and the informal negotiations took place in a context of growing economic problems which exerted a considerable influence over the Government's plans. It is sufficient to mention only two here.

Firstly, there was a hiatus in investment in the North Sea from 1974 to 1976. During this period the capital invested by licensee companies in the development of proven fields was reduced to nil. By contrast, exploration continued and indeed proved highly successful. In the first ten months of 1975 more exploration wells were drilled than in the whole of 1974. The success rate of 1 in every 3 wells drilled was unusually high, and a dozen probable fields were established.<sup>1</sup>

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1. Department of Energy, Development of the oil and gas resources of the United Kingdom (the 'Brown Book') (1976).

In spite of this, a picture was emerging in late 1974 of a 'loss of confidence' on the part of licensees and their bankers. The initial optimism about North Sea prospects was rapidly giving way to a mood of pessimism which was to last until mid-1976.

The principal reason for this development was a rapid escalation of costs: to put it another way, there was a decline in expected future profits. Throughout 1974, costs had arisen sharply, adding hundreds of millions of pounds to original investment forecasts. For example, the estimated cost of developing the Forties Field was claimed to have risen from £350 million in 1972 to £750 million in mid-1975.<sup>1</sup> This development and its possible consequences for the future exploitation of oil resources was considered so serious by the Government that it initiated a study into cost escalation in June 1975. However, the report by a Department of Energy study group concluded that a large part of the cost escalation problem was the result of inadequate forecasts by the oil companies at the initial stage.<sup>2</sup>

The Report also stated that

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1. North Sea costs escalation study, op.cit., p.2. Both capital and operating costs continued to increase for some time. For example, the stockbrokers Wood Mackenzie estimated that in 1978 the operating costs for some fields doubled, and capital costs increased by as much as 43 per cent: cit. in The Financial Times, Year's operating cost 'doubled in some North Sea oilfields', November 11, 1978.
  2. North Sea costs escalation study, op.cit., p.18. The combination of an initial under-estimation of the harsh environmental conditions and the technical challenges on the one hand, with the rapid time-scale which companies set for their projects on the other, contributed significantly to the problem. The study was



... as long as oil companies are negotiating with the Government their public statements on the future consequences of cost escalation are likely to reflect a bargaining position.<sup>1</sup>

It added:

It is clear that escalation as defined and indeed absolute future increases in costs will not be determined by action or inaction on the part of the Government.<sup>2</sup>

Neither Government policy nor the proposed legislative changes were likely to have any significant impact on the escalation of cost. However, the oil companies chose to present a different picture.

It was alleged that

'... excessive Government intervention' was making 'the task of oil companies in a troubled period more difficult'.<sup>3</sup>

The Vice-President of Conoco, an American oil company, made sweeping criticisms of Government policy in a paper given at a Financial Times Conference and widely reported at the time.<sup>4</sup>

In his paper entitled 'Why are we still here?' Mr. G. Maier identified several reasons for the mood of pessimism affecting licensees and their bankers. Apart from the escalation in cost, there

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1. op.cit., p.19.

2. loc.cit.

3. Dr. A.W. Pearce, Chairman of Esso Petroleum, in the company's annual report for 1974-5, published April 1975. Cit. in The Financial Times, Esso and BP attack North Sea oil policy, April 12, 1975.

4. For example, The Guardian: Uncertainty 'could force firms to quit North Sea exploration', December 12, 1974.

was a scarcity of necessary materials and equipment, and the world recession was having an impact in the North Sea. For example, high rates of interest (up to 13%) were adding to development costs. In addition, the capital market was in a 'depressed state', making financing difficult.

He identified three other reasons. Firstly, suppliers and fabricators quoted long delivery times and failed to meet delivery deadlines, which extended the time taken by projects to be completed and to generate revenue. Secondly, he claimed that the results of exploration drilling were not as promising as they appeared. Offshore areas which had been thought to contain considerable reserves had produced disappointing results when delineation wells had been drilled. (This suggestion 'coincided' with an announcement by BP of a second dry well west of the Shetlands.)

Finally, he warned that if crude oil prices declined (as they did in real terms until 1979), existing projects might prove 'uneconomic'.

It was into this situation of uncertainty that the Government's proposed measures were cast. Maier declared that

The industry's confidence has<sup>8</sup> been shaken by uncertainty about Government action on taxes, definitions of majority participation, and revisions to existing licence terms.<sup>1</sup>

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1. G. Maier, Why are we still here?; paper given at a Financial Times North Sea Oil Conference, and reported in The Guardian, 'Uncertainty', op.cit. Maier claimed that inflation had increased costs by 50 per cent within six months of commitment of capital in one project in which Conoco were involved. In the context of 'uncertainty', see also the discussion in The Financial Times, Killing industry faith in Government fairness, September 20, 1974.



The implication was clear: the adverse economic situation was unavoidable but the actions of the Government were worsening that situation and were doing so unnecessarily.

The consequences were spelled out by a leading American banker, who said

Unless some problems are solved fast, I can see the date when Britain becomes self-sufficient in oil slipping back from the Government target of 1980 to anywhere between 1981 and 1985.<sup>1</sup>

This idea of a close connection between Government policy and the climate of 'uncertainty' was also exploited by the Conservative Party. Mrs. Thatcher was particularly critical of the 'uncertainty' allegedly produced by the Government's participation plans.<sup>2</sup>

The Government certainly took the threat of retrenchment seriously. Although the oil companies had already committed large sums of capital to the North Sea, many fields were still at the pre-production stage and required the injection of further large sums of capital before their proven reserves could be developed, and self-sufficiency reached by 1980. It therefore gave assurances to the licensees at regular intervals from 1974 to 1976 to the effect that the Government's plans would not preclude a high rate of return for companies developing North Sea fields. For example, on the very day that Mr. Maier gave his paper, two Ministers from the Department of Energy made

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1. Ed Monteith, reported in The Sunday Times, 'Oilmen push for deal they cannot lose', July 20, 1975.
  2. For example, her remarks reported in The Financial Times, 'Mrs. Thatcher facing US questions on North Sea oil', September 15, 1975.

speeches designed to reassure the oil industry about the impact of state participation.<sup>1</sup>

However, criticism of the Government proposals was not the only means of persuasion at the oil companies' disposal. They could use their considerable economic power to freeze plans for the development of existing fields and to reduce their exploration drilling. There is some evidence that they did both. Some senior executives in the oil industry certainly thought that this happened.

The chairman of one of the world's largest oilrig operating companies, Mr. A.J. Laborde, claimed that the oil companies had decided to 'pull back' as they awaited clarification of the Government's plans. He claimed that some oil companies appeared to be delaying North Sea development as part of a deliberate negotiating tactic. Major oil companies were 'curtailing operations and tightening budgets', and his company was one of a number which were 'pulling rigs out'.<sup>2</sup>

A managing director of British Petroleum, Mr. Monty Pennell, specifically rebutted Government claims that the 'companies are bluffing when they talk of reducing exploration drilling in the North Sea' and suggested that the actual rate of drilling could fall by as much as 60% in 1975. He added:

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1. See The Guardian report, 'Uncertainty', op.cit.
2. Oil rig chief rejects Ross's North Sea reassurance, in The Financial Times, September 17, 1975.



Politicians who look to the current rate of drilling appear not to understand that rig activity today results from decisions taken a couple of years or more ago; and that decisions taken over the past few months will largely determine the rig activity next year.<sup>1</sup>

Such statements hardly make a case for suggesting that the hiatus was little more than an 'investment strike' by the oil companies and I shall not attempt to make such a case.<sup>2</sup> However, they do suggest that some exercise of economic power was used by the oil companies to prolong the hiatus and influence their negotiations with the Government, particularly on the question of state participation. In addition, at least one of the reasons given by Mr. Maier for the hiatus lacks credibility.

The argument that financing was proving difficult due to the escalation of costs did not hold with respect to the major oil companies. Such companies were able to finance field development largely from their own funds.<sup>3</sup> Where this proved impossible, they were able to borrow without difficulty from the larger banks since their credit rating was high. As one writer notes:

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1. Esso and BP attack North Sea oil policy, in The Financial Times, April 12, 1972.
  2. For a brief discussion of 'investment strikes' see Paul Mattick, Marx and Keynes, p.14. 'There have been times', Mattick says, 'when capitalists have refused to take 'risks'; when instead of investing their and other people's money they have held on to it, an attitude which Keynes calls "liquidity-preference".'
  3. One study of seven international oil companies showed that in the past five years some 83% of their capital expenditure of over £15,000m. had been financed from depreciation and retained earnings. These companies would produce at least 70% of British sector North Sea oil by 1980-2: see 'The honeymoon period is now over', in The Investors' Chronicle, August 30, 1974.

Whatever one may say about imperfections in the capital market and the risks of oil exploration, it cannot be denied that the large companies involved have some of the best credit ratings to be found.<sup>1</sup>

In addition, the major oil companies had never subscribed to the highly optimistic predictions commonly made in 1972-4.<sup>2</sup> They had accepted that a slowing down of the pace would develop as the giant fields discovered at an early stage gave way to smaller structures, not so easy to drill and requiring more wells. Experience showed that such a development was inevitable.<sup>3</sup>

The escalation of costs and generally adverse economic conditions had a different impact upon companies smaller than the majors. For such companies, the words of one banker had a special relevance. As early as August 1974, Angus Grossart claimed that

There are clear signs that money, whether in the form of equity or debt finance is becoming scarce and that investors and bankers are taking a much tougher line on the equation which they are drawing between risk and reward and on the terms on which they will supply money.<sup>4</sup>

The banks were urged to 'participate more actively in the profitability of projects'.<sup>5</sup>

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1. Dam, Oil Resources, p.32.

2. See, for example, North Sea Reports, a survey, in The Investors' Chronicle, May 3, 1974, p.5: 'The North Sea adventure could become Britain's greatest industrial revolution'; also 'Introduction' to Casenove & Co., The North Sea, op.cit. Apparently, North Sea gas was seen as playing a regenerative role rather earlier, see Adelman, op.cit., p.241.

3. This view has been set out by the UKOOA, in their submission to the Energy Commission: 'Exploration and Development of UK Continental Shelf Oil', October 1978.

4. The honeymoon period is now over, in The Investors' Chronicle, August 30, 1974.

5. Ewan Brown of the merchant bank, Noble Grossart, reported in The Scotsman, 'Risk more on oil, banks urged', October 9, 1974.



Such an insecure relationship to sources of finance was not a general condition for companies operating in the North Sea. Given their ability to finance development from internal sources, and their close links with the larger banks,<sup>1</sup> the oil majors were in an entirely different position. The sharp escalation in costs came as no surprise to them since they had not subscribed to the initial optimism; and their access to sources of finance virtually eliminated problems in financing field development of the sort which smaller companies certainly did experience.

There was one other economic development which had an impact upon the Government's proposed legislation: the development of a 'fiscal crisis' of the state from 1974 onward.<sup>2</sup>

The scale of Government borrowing increased considerably during this period and, at the same time, the large increases in oil prices in 1973-4 exacerbated existing balance of payments difficulties for the UK. The prospect of revenue from North Sea oil was essential for state finance since this prospect allowed the Government to secure loans to meet its current expenditure, and solve the balance of payments problems. In addition, this lack of financial resources precluded money compensation for those companies affected by changes in existing licence terms, and acted as a constraint upon the form of state participation.

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1. See chapter one, section 2.
2. For an elaboration of this idea of fiscal crisis, see James O'Connor, The Fiscal Crisis of the State, pp.1-10.

While it was to the oil companies' advantage to exploit the dependence of the Government upon future oil revenues, that dependence was not of their own making. So long as the Government adhered to the objective of self-sufficiency by 1980, it remained dependent upon the oil companies' control over capital for the further investment required to meet this objective.

### 3. The debate in Parliament

While the informal negotiations between the Government and oil companies took place in the Department of Energy, the public debate began in Parliament. This proved to be a highly controversial and often heated debate, which gave rise to some considerable disagreement between the House of Commons and the House of Lords, and which led to substantial modification of some of the key provisions in the Petroleum and Submarine Pipe-Lines Bill.

Part II of the Bill concerned the terms of petroleum production licences, and the proposed new regulations for seaward areas were set out in Schedule 2. They proposed inter alia to confer upon the Secretary of State for Energy wide discretionary powers, the most significant of which were the following:

(1) a power to control the level of production in each field. The new model clauses 15 and 16 would have allowed the Minister to tell a licensee not to produce oil from a particular field if he considered that too much oil was being produced from the North Sea

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as a whole. This had obvious implications for companies' expectations of future profits, and for smaller companies' ability to obtain loans.

(ii) a power to revoke any licence in toto in the event of a breach, even if the breach occurred in one small part of the licensed area (model clause 39). Clearly, instant revocation for minor breaches would have contributed greatly to the insecurity of a licensee's interest.

(iii) a power to impose additional exploration programmes after the initial six year term of the licence (model clause 14). The exercise of such a power would impose additional cost on a licensee and might prove unprofitable. Model Clause 15 might have had a similar effect with respect to development. These were supplemented by others like the power to regulate more strictly any dealings in licence interests (model clause 38), to restrict the flaring of natural gas (model clause 21), and powers over the rate and form of royalty payments (model clauses 9, 10 and 11).

The sheer quantity of regulation contained in the new model clauses (which would of course replace those in existing licences once the Bill was enacted) seemed to justify the Government's claim that it was providing the necessary 'public control' which its predecessors had failed to provide. While in a sense it was indeed an extension of 'public control', the form of this 'public control' was one quite compatible with, and perhaps even necessary for, the

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continuation of profitable economic activity by private companies in the North Sea. There were, nonetheless, considerable conflicts in Parliament as the Opposition attempted to fetter these discretionary powers, when they could not persuade the Government to remove them: one of their successes in this respect was the proposed power to control the level of production. For the rest of this section I examine the ways in which some key regulatory powers in the Bill were amended and their consequences, with particular reference to depletion-control, the most important regulatory measure of all.

(1) The power to control the rate of production

Depletion or production controls are a standard part of the legislation of most oil-producing countries and even of countries which have no oil production but which are merely trying to encourage exploitation. Prior to 1974 however, no policy on depletion seems to have existed in Britain nor did Governments have any explicit powers to control rates of depletion under the terms of production licences awarded before that time: in other words, in the first four rounds of licensing.

The need for depletion control stems from the physical character of oil as a finite, non-renewable resource which is not merely produced but at the same time used up. Once it is extracted and consumed either directly as fuel or indirectly as raw material in, for example, the production of synthetic fibres, the oil is 'depleted'. In this sense depletion simply means the production of a non-renewable natural resource, but the word also conveys the

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idea that this production process has a negative aspect. It is this feature which gives all the parties involved an interest in the rate and manner of depletion. However, whereas states tend to want such controls in order to prolong the life of their oilfields (and the benefits therefrom), there are at least two reasons why oil companies should be much less interested in controlling the rate at which oil is to be depleted. Firstly, as private companies they produce oil for their own profit, and the quickest way to make the maximum profit in the short-term is to deplete the oil fast. Secondly, the high cost of exploration and development in offshore areas and the long period between initial investment and actual production has encouraged oil companies to recoup their investment as fast as possible. After all, the sums involved are massive: an exploration well can cost between three and five million pounds (i.e. the equivalent of purchasing a small jet aeroplane such as a BAC 1-11), and the cost of developing a medium-sized oilfield is between £500 million and £1,500 million (similar to the cost of the entire Concorde project up to July 1977, i.e. £820 million).<sup>1</sup> As a consequence of these considerations, oil companies tend to view the depletion powers of states as potential threats to their future rates of profit.

There is then a possible divergence of oil company interests from that of the nation-state in whose territory the oil lies.

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1. Figures are from Proceedings, op.cit., vol.I, at p.13.3. A general account of depletion control offshore is contained in the Ministry of Industry's Report (No. 30) to the Norwegian Storting (1973-4), pp.64 et seq.

In Britain's case, this has been minimal however. During the initial phase of oil and gas exploitation up till 1974, Government policy had been directed at stimulating exploration activity and achieving as rapid a build-up of petroleum production as possible. One of the effects of this policy was that licencees were allowed to produce from gas fields with very few restrictions and to plan to exploit oilfields in the same way, i.e. without any significant state interference in this respect. Apart from controls on the drilling of wells, set out in Model Clause 13 of the Petroleum (Production) Regulations 1966, the manner of exploitation was left entirely to the licencees.<sup>1</sup> This suggests that in so far as depletion rates were considered at all, it was assumed that the oil companies' interests and goals would coincide with the 'national interest', an assumption by no means unjustified.

The new oil policy of the Labour Government seemed to imply an end to this coincidence of interest between the state and the oil companies on the question of production control. A major objective of this policy was to assume powers to control rates of production in the North Sea oilfields<sup>2</sup> in order to deal with a range of possible future problems which could not be clearly

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1. The Mineral Workings (Offshore Installations) Act 1971 changed this a little: under this Act, extensive regulations were promulgated to promote good oilfield practice and safety in operations.
  2. For example, in the Election Manifesto of October 1974 the Labour Party claimed that a Labour Government would 'take new powers to control the pace of depletion' (p.12).



gauged in 1974, but which would arise once 'self-sufficiency' was reached in 1980. On the other hand, the oil companies and their bankers needed the maximum degree of 'certainty' for the large investment decisions involved in field development. Consequently, the licensees were quick to criticise the apparent lack of restrictions on the Government powers implied by the phrase 'to control the level of production in the national interest' contained in the White Paper of July, 1974.

The oil companies envisaged a situation in which a British Government could prevent a consortium from developing a field or could compel an amendment of production plans once fields were already in production, thus jeopardising the security of their existing investment as well as their ability to raise capital for future investment. In addition, there was a certain amount of anxiety over the possible exercise of such a power in a discriminatory way among the various licensees.

So alarmed was the Government by oil companies' criticisms that it acted firmly before legislation was introduced into Parliament. After consultations with the companies, the Energy Secretary, Mr. Eric Varley, made a statement in Parliament in December 1974, which was intended to assure them about the Government's intentions.<sup>1</sup> Although they were not incorporated into the Petroleum and Submarine Pipe-Lines Bill and therefore not legally binding, the

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1. 882 H.C. Deb. cols.648-50 (December 6, 1974) (Written Answer). The following passages are taken from this statement.

Varley Assurances provided the background to the Bill's provisions on depletion-control and complemented them.

To begin with, Mr. Varley assured the oil companies and the banks (on which some oil companies were highly dependent for finance) that

Our depletion policy and our implementation (i.e. of election commitments) will not undermine the basis on which they have made plans and entered into commitments.

However, a general power was necessary to ensure that the oil would be used at a rate which secured the greatest benefit to the British economy in the long-term. Of course the Government could not define its long-term production policy before any oil had been produced and while large offshore areas remained unexplored, but it remained committed to rapid development until 1980. For the benefit of holders of licences allocated in the first four rounds, he set out the following guidelines which were to form the basis for depletion policy, with the expectation that these would illustrate the limits upon the exercise of the Government's proposed power:

1. Discoveries made before the end of 1975 under existing licences would not be subject to delays imposed upon their development plans. Cuts in production from discoveries made before the end of 1975 under existing licences would not be made before 1982 or four years after the start of production, whichever was the later. This had the effect of stimulating companies to make

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faster progress on their exploration programmes.

2. Discoveries made after the end of 1975 under existing licences would suffer no production cuts before 150% of the capital investment in the field had been recovered.

3. Should it prove necessary to delay the development of any discoveries made after the end of 1975, this would only be done after 'full consultation with the companies so that premature investment is avoided'.

4. In general, any use of production controls by the Government would recognise 'the technical and commercial aspects of the fields in question'. This would generally restrict production cuts to no more than 20%, and the industry would be consulted on the period of notice to be given before cuts became effective.

In spite of these specific assurances the power over depletion rates set out in the Petroleum and Submarine Pipe-lines Bill was so broad as to provoke renewed criticism. Model Clauses 15 and 16 in Schedule 2 (which were to apply to existing as well as future licences) proposed to give the Minister a virtually unlimited power to vary production plans, and to set maximum or minimum production-rates. It appeared that the Minister could determine any output rate he wished and there were no constraints on his ability to alter production rates since he could 'specify any rate by reference to such factors as the Minister thinks fit'.<sup>1</sup>

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1. Model Clause 16 (3)(a).

The absence of any provision for appeal provoked some criticism: he had only to allow the licensee to make representations and then satisfy himself that his decision was 'in the national interest' before exercising his power.

However, there were two criticisms of this power made by the Conservative Party: one general and one particular. The general criticism was a variation on the one they repeated at every stage of the Bill's passage through Parliament, attacking the Government's stated intention to introduce the new model clauses into existing licences by legislation. The Opposition made it clear that they were not opposed to the taking of a power to control rates of production,<sup>1</sup> but they did object to the inclusion of any such power in the regulations of licences already allocated. These licences had a contractual character and therefore the Government ought to find an alternative means of taking a power over existing licences, or else negotiate with the licensees over compensation for its inclusion. When the Government nonetheless maintained that their procedure was quite 'normal' and had similar consequences for property rights as a change in the tax environment, the Opposition (rightly) pointed out that this view was quite mistaken. However, this particular criticism had as little success with regard to the Bill's provisions on depletion-control as it had with any other provisions of the Bill.

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1. 'There must be somewhere in our legislation effective controls on the rate of depletion.': H.C. Deb. Standing Committee D, col.1128 (July 3, 1975); although they thought a state regulatory authority was required: 891 H.C. Deb. col.503 (April 30, 1975).



The Opposition had much more success with their specific criticism that the power set out in the Bill was apparently unfettered and too general in character. Ironically, Model Clause 16 was taken out in Committee and a new (rewritten) Model Clause introduced as a result of a Government amendment made to placate criticisms from the oil companies in the private consultations which were taking place simultaneously. By the time the Conservative Party made their criticisms of this power in detail, the Government spokesman, Mr. John Smith, was able to claim that these criticisms had already been met and that at least one head of a major oil company had agreed that the provisions in the new Model Clause were 'reasonable provisions'.<sup>1</sup>

The new clause introduced a system of 'limitation notices' which were designed to provide licensees with some security about the use of Ministerial power. When the Minister approved a development programme he would also issue a limitation notice specifying the maximum amount of cut-back in production which he can subsequently enforce. This way the Minister retained the effective power to cut back production, while the oil companies and the banks know before any capital is advanced the limits on the exercise of that power and therefore, in so far as it is affected by depletion control, the minimum profitability of the oilfield. In the same clause were new provisions concerning

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1. H.C. Deb. Standing Committee D cols.1338, 1346-49 (July 8, 1975).

the Minister's power to increase production, which emphasised that this would only be used during a national emergency and that any costs incurred by the licensee would not exceed the cost of drilling a new well. This allowed the industry to appreciate clearly that only a minor investment would be involved in these exceptional circumstances, without reducing the Government's ability to act in the national interest. In addition, there had to be advance notice of any intention to vary production within the limits specified by the limitation notice and this 'further notice' must also specify limits. The effect of all this was to provide licensee companies with a guaranteed floor rate of production, thus protecting their profitability.

These new provisions, setting out procedural limits to the exercise of the Secretary of State's power, supplemented the substantive limitations set out in the Varley Assurances. An assurance was given that the guidelines set out by Mr. Varley were still in operation. Together, they had the effect of limiting the practical consequences of the Government's power by ensuring that it would not be used with respect to oilfields discovered under pre-1974 licences until 1982, and if used at all in the 1980s it would not have more than a minimal effect on profitability for the licensees concerned.

The importance of the Government's proposed power over

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depletion-rates was, as Proudhon said about property, 'clear to all minds'. It was 'one of the most important features of the Bill',<sup>1</sup> and formed 'the heart of the licence changes'.<sup>2</sup>

According to Mr. Varley,

The need for retrospectivity arises only because in 1971 no depletion powers were taken in the licences.<sup>3</sup>

Similarly, the oil companies treated this provision as among the most important in terms of its implications for company profitability. The chairman of the Esso Petroleum Company, for example, publicly stated that

The economic consequences of producing well below the levels for which installations were planned are very serious unless there are compensating correctives (sic).<sup>4</sup>

Its implications for field profitability in the short-term were not the most important consideration, so far as the oil companies were concerned. The real importance of the depletion power was located in one vital fact: North Sea oil reserves were small by global standards and might run out before the end of the century. As a consequence of this, British Governments would, sooner or later, use the depletion power to extend the life of a number of oilfields. The precise form of the new power was therefore a matter of some consequence to the oil companies in the longer-term.

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1. Patrick Jenkin in H.C. Deb. Standing Committee D, col.1332 (July 8, 1975).

2. John Smith, loc.cit. at col.1122 (July 3, 1975).

3. 891 H.C. Deb. col.505 (April 30, 1975).

4. The Guardian, 'A field where oil firms "know best"', June 19, 1975.

Nonetheless, in spite of the political rhetoric, what is most striking about the debate on this most important provision is the degree of consensus between the two parties, which ultimately extended <sup>to</sup> the licensees themselves. Neither the licensees nor the Conservative Party thought there was anything objectionable about the Government's acquisition of a reserve power per se. Most oil producing states already had such a power, and the oil companies made it known to MPs that some form of control of production would be 'totally within their understanding of the reasonable activities of Government'.<sup>1</sup> The chairman of Esso emphasised the need for 'the most careful management of oil and gas reserves to prolong their economic life',<sup>2</sup> while BP even suggested that a regulatory commission be established, charged with conservation policies and, where necessary, pro rationing.<sup>3</sup> So far as the major political parties were concerned, both appreciated the importance of a reserve power over domestic oil production since the debate on the Bill took place in the context of a radical change in the world oil market: fears of an impending shortage of energy and non-renewable physical resources were growing and prices of such resources were expected to rise further.

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1. John Davies MP at 891 H.C. Deb. col.518 (April 30, 1975); see also H.C. Deb. Standing Committee D, cols.1129-30 (July 3, 1975).
  2. The Guardian, 'A field where oil firms "know best"', June 19, 1975.
  3. NISC, op.cit., Memorandum submitted by BP, pp.106-7. 'Pro rationing' is a technical term which simply means the limitation of production from an oilfield at a certain stage of its 'life'.



Agreement must have been further facilitated by the fact that the exercise of depletion controls was highly improbable before 1980 when self-sufficiency would be reached. As one financial journal bluntly put it,

These oil companies, their bankers, and the financially nervous Government have one vital interest in common: they all want to get the oil out of the ground as fast as possible.

The Labour Government, like its Conservative predecessors, was committed to rapid development to realise tax benefits, royalty revenues, to improve the balance of payments, and to obtain security of oil supplies. It is not particularly remarkable then that, several years later, the Government which has chosen to exercise the power of depletion control in 1980, as a Labour one might have done, should instead be a Conservative one.<sup>2</sup>

(ii) Other regulatory powers

The form taken by the other new powers also showed the influence of the Government's informal discussions with the industry. At the same time they highlighted the contradiction of a state presenting itself as a 'private' party re-negotiating an unfair deal and yet taking regulatory powers which only a state would want.

The power of revocation contained in Model Clause 39 was an example of this. In the event of a breach in licence obligations, the Energy Secretary would have the power to revoke the licence in toto.

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1. The Banker, May 1977, p.73: 'Over the hump'.

2. The Financial Times, 'Government plans to delay oil field development', July 24, 1980.

There was no apparent qualification to this power and hence revocation was possible even when a breach had occurred in one small part of the licenced area. As a consequence it was sharply criticised by licensees and Conservative spokesmen, who sketched model scenarios in which total revocation might occur for relatively minor breaches. In addition, since some individual licences covered several blocks and more than one oilfield, there were fears that a breach by one party might lead to revocation of the whole licence, thus affecting the interests of all parties and perhaps the actual development of an oilfield.

Initially, the Government thought that assurances about its exercise would still the criticism, and Lord Balogh announced that

There was no question of holding the threat of total revocation like a sword of Damocles over the heads of licensees to force them to undertake unreasonable investment.

However, the exercise of such a power would have too great an impact on company plans for licensees to view with magnanimity its broad discretionary character. While they made their disquiet known to Ministers in the informal consultations, the Conservative Party proceeded to make a connection between the much publicised hold-up in field development and the 'threat' of revocation: it was alleged to be partly responsible for 'detering

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1. 364 H.L. Deb. col.884 (October 15, 1975).



companies from embarking on offshore operations'.<sup>1</sup> The Government soon came to accept the Lords' view that the companies needed firmer guarantees, and tabled amendments at the Report stage which ensured that if there was a breach of the licence terms in respect of a programme under Model Clause 15 (concerning the development of oilfields), the Secretary of State would not be able to exercise his power of revocation so as to deprive a licensee of a commercial field in another part of the licensed area where there had been no such breach.<sup>2</sup> A provision was also made for the licensee to make representations to the Minister prior to the taking of any decisions with which the licensee might find it difficult to comply: for example, the altering of a licensee's production proposals.<sup>3</sup> Provision was also made for a period of delay before revocation during which the licensee might correct a change of control (resulting from assignment of a licence interest) which the Minister did not approve of.<sup>4</sup> Finally, the Minister was given a discretion to make a partial revocation instead of a total one, if the licensee had failed to comply with exploration, development or production programmes.<sup>5</sup>

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1. 364 H.L. Deb. col.589 (September 25, 1975).
2. Petroleum and Submarine Pipe-lines Act, Schedule 2 (cited below as 'Act') Model Clause 16(8).
3. Act, Model Clause 15(7).
4. Act, Model Clause 39(3)(c).
5. Act, Model Clauses 14(6) and 16(9). Their fear was that the power to revoke would be used in conjunction with the power to impose additional exploration or development programmes. A modification in model clause 14 ensured that any additional exploration programmes 'will only be those which a conscientious licensee with adequate resources would carry out of his own accord to maximise his commercial advantage', John Smith, H.C. Deb. Standing Committee D, at col.1239 (July 3, 1975).

The modifications to the power of sanction had the effect of mollifying the other new powers over exploration and development programmes. Ultimately, it qualified the Minister's ability to enforce the exercise of discretionary power with respect to the most important new model clauses, and thus minimised their impact on the terms of existing licences. Nonetheless, the Minister retains a power to revoke the licence, and this was consistent with the Government's general objective of ensuring that reserve powers over all stages of field development were held by the state.

Other regulatory powers were important in a technical and less controversial sense. For example, companies might be compelled by the Minister to develop a field which covered several licences as one unit, thus organising different private interests and avoiding wasteful competition.<sup>1</sup> The Government also took the power to demand its royalties in the form of oil rather than cash, amended in Parliament to oblige the Minister to take into account the disturbance that might be caused to an operator's drilling and delivery arrangements in this eventuality.<sup>2</sup> Both of these are common worldwide, as is the most important 'technical' power of all: the power to control an assignment of licence interests.

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1. Act, Model Clauses 25, 26.

2. Act, Model Clause 11.



Strict restrictions on assignments had been present from the outset of North Sea exploration, providing that a licensee should not without consent

... assign or part with any of the rights granted by this licence in relation to the whole or any part of the licensed area or grant any sub-licence in respect of any such rights.<sup>1</sup>

However, the massive expansion of activity on the UK Continental Shelf had revealed this simple prohibition to be insufficient and 'new complex provisions were introduced in model clause 38 of the Bill. The principal objective was to prevent a situation in which a Minister could award a licence to a company owned and operated by one person or group A and later discover it had been turned over to a company owned and operated by quite another person or group B 'who may be of a different nationality', all without the Minister's knowledge.<sup>2</sup>

While this was an important clause it was not especially controversial. The Conservative Government had imposed an effective embargo on the transfer of licence interests in November 1973 from which time no future transfers had been made until February 1975. A market had been developing in licence interests subsequent to the fourth round of allocation, and they had recognised that existing state regulation was inadequate. The

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1. Model Clause 32 of the Petroleum (Production) Regulations 1966, S.I 1966 No.898, Schedule 4.

2. 891 H.C. Deb. col.492 (April 30, 1975).

oil companies also appreciated the need for regulation in this case, and all parties wanted a speedy resolution of the problem. The escalating cost of North Sea activities left some companies short of the necessary capital to pay for their share of the work: in these circumstances they would normally 'farm-out' or exchange an interest in the licence with another company in return for the performance of work, usually the drilling of a well or wells. Since February 1975, fourteen companies involving 40 licences had applied to the Department of Energy for various assignment projects.<sup>1</sup> The informal discussions, supplementing the debate in Parliament ensured that new regulatory controls could be introduced which would be truly effective and would satisfy all the parties involved.

#### 4. The meaning of 'unilateral'

From the foregoing it is clear that the terms of existing licences were revised as the result of a unilateral decision taken by the British Government, but that they were not revised unilaterally. The procedure adopted by the Government was intended to allow for, and indeed to encourage, maximum discussion and amendment to its proposed legislation. As a result, the new model clauses introduced into the terms of existing licences had no discernible adverse impact upon the economic interest of these licensees.

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1. 365 H.L. Deb. col.1776 (November 11, 1975). A general account of the legal aspects of assignment is contained in 'Farm-Ins and Farm-Outs' by Andrew W.A. Berkeley in Proceedings (Paper 17).



This conclusion is less surprising when one considers, firstly, the state's role in North Sea oil development in the longer term (since 1964), and, secondly, the international context in which the Government's action was situated.

The regulations contained in the model clauses of production licences allocated in the first four rounds had been drawn up on the assumption that if there were oil resources in the North Sea, they were not likely to exist in very large quantities: even if there were large quantities these would surely take a long time to be produced from the difficult conditions of the North Sea. However, by 1974 many fields had already been proved to contain recoverable reserves and several had reached the development stage. Production on a large scale was certain to begin well before the end of the decade. In this context the existing body of regulation seemed both too simple and too sparse to permit the performance of the economic administration and co-ordination which had been typical functions of the state from 1974 onward, albeit on a very small scale.

This was perceived as a problem both by the two major political parties and by the oil companies themselves. As I explained in chapter one, a large element of economic regulation is both necessary and commonplace in the oil industry, and is introduced by the private oil companies, especially the major ones, as well as by the state.<sup>1</sup> However, the growing scale of North Sea activity

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1. The best example of this self-regulation is the operating agreement, which *inter alia* determines the respective shares of the companies involved in the licence; provides for the appointment of one of them as operator, as well as his responsibilities to and control by the other licensees; regulates the financial contributions of the licensees and their taking of their entitlement to oil; and generally provides for all matters essential to the interests of the parties in exploration, development and production activities.

and the imminence of actual production presented complex problems of regulation and co-ordination which the private companies could not solve themselves - nor did they expect to. A public interest was required to provide further elements of co-ordination among the diverse private interests which they could not provide themselves. Since 1973, the Conservative Party had been considering new rules which would allow for an increase in state regulation of North Sea developments. The Labour Party of course came to power in 1974 with a general mandate to introduce new rules on this matter. Not surprisingly, when the Labour Government made their legislative proposals known to the oil companies, the reaction was far from hostile. The Government was congratulated for coming forward with

Legislative measures clearly aimed at ensuring, rather than undermining, <sup>1</sup>the commerciality of the operations in British waters.

Apparently, many of the larger oil companies recognised that

... a tightening up along these lines is inevitable and not intrinsically against their interests.<sup>2</sup>

Indeed, the regulatory provisions of the Bill could be regarded as

No more than the back-up powers over the rate and manner in which its natural resources are used, which any state must have at its disposal.<sup>3</sup>

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1. Cit. in H.C. Deb. Standing Committee D, col.1163 (July 3, 1975). Mr. Benn mistakenly refers to 'The Petroleum Economist', but he means 'The Petroleum Times'.
  2. The Financial Times, 'Killing industry faith in Government fairness', September 20, 1974.
  3. The Financial Times, 'North Sea oil: political games that miss the mark', April 12, 1975.



This favourable view of the proposed regulatory measures did not extend to the proposed introduction of majority state participation into existing licences, and the critical attacks directed at that were usually assumed to extend to the former. As a negotiating tactic, the oil companies took no trouble to disagree with this.

The disagreement began with the precise form of the required regulation and above all the manner in which it was to be introduced. The fact that meaningful changes would have to be directed at the terms of licences already allocated was no doubt partly the reason for the Conservative Government's inability or unwillingness to make any substantial changes throughout the period when they were conducting a review of licensing policy: that is, from 1972 to 1974. Whatever the economic benefits of such a course, the use of sovereign power to amend the existing regulatory controls was unacceptable to them. The Labour Government made a very different estimate of the situation and proceeded to provide the first legal framework of regulation designed to apply specifically to the exploration and exploitation of offshore oil in the UK.

It is ironic, however, that the very Government which took the decision unilaterally to initiate a revision of existing licences should have denied so consistently that its step was an unusual one. Government spokesmen consistently professed to see no difference between this action and the alteration of regulatory or fiscal measures with the effect of making contracts more onerous

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(the second mode of procedure outlined in s.1). In an exchange with Mr. Jenkin at the Bill's Committee stage, the Energy Secretary, Mr. Benn, argued that Parliament could, and often did, alter the legal framework within which property rights are exercised (in taxation, for example), and this was what they were in fact doing.<sup>1</sup> However, this was not in fact what they were doing, since contracts which had been entered into for a number of years and from which derived rights to property in oil 'won and saved', were being broken. The Government was not then attempting to alter the legal framework within which those rights were exercised. No contractual obligation was involved in the cases Mr. Benn had in mind: for example, the enactment of the Mineral Workings (Offshore Installations) Act 1971 had the effect of making existing licences less attractive by reducing their value, but it did so only incidentally by altering the regulatory framework in general: indeed, the oil industry did not oppose the Act and recognised the need for it. Nor was the measure comparable to changes in taxation announced in a Budget since such changes have a general character and are not limited to a particular kind of industry. What the Government proposed to do was not 'normal', as both Mr. Benn and, in the House of Lords, Lord Balogh claimed.<sup>2</sup>

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1. H.C. Deb. Standing Committee D, cols.1146-72 (July 3, 1975); see also 899 H.C. Deb. cols.465-82 (November 5, 1975).

2. 364 H.L. Deb. cols.551-572 (September 25, 1975).



The Government's mode of procedure was not of course unconstitutional. The notion that Parliament is unable to bind itself restricts the capacity of the Crown to validly contract so as to fetter its future executive action,<sup>1</sup> and hence in municipal law there was no formal barrier to the Government's course of action. The state might be seen as having a moral obligation to the licensee not to change the terms of the licence once awarded but it could not have a legal obligation. Hence it might be concluded that, formally at least, a licensee in the United Kingdom has much less protection than in Norway where there exists a system of judicial review on the Supreme Court model.

Nonetheless, in 1974 the Government was very uneasy about the legislative procedure it had chosen. Reference to the international context of its action immediately provides an explanation for this unease, and here one can discern more elements of historical continuity in policy-making (i.e. since 1964). Once again law and policy were significantly influenced both by the international operations of a powerful sector of the British economy and by Britain's role of 'junior partner' in a 'special relationship' with the United States. Not only were there many American companies operating in the North Sea who

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1. Rederiaktiebolaget Amphitrite v. the King, [1921] 3 K.B. 500.

were likely to be affected by the Government's legislation but their projected rates of profit were very high. For example, by the early 1980s, Exxon was <sup>X</sup>expecting a net cash flow, after all British taxes, of \$350 million a year from the Brent field alone.<sup>1</sup> Similarly, the British Petroleum Company <sup>high expectations of high rates of return on their</sup> had highly profitable activities in the United States, and Senator Dole of Kansas was quick to draw this conclusion:

As I look at the billions of barrels of American oil which the British Petroleum Company is sitting on in Alaska, when I consider the holdings of the Shell Oil Company in the United States, it seems to me that these and similar holdings must be considered as the British programme to nationalise the petrol contracted for by American companies in Great Britain goes forward.<sup>2</sup>

The Republican Senator was not musing idly, nor were the fears of the British Government on this score unfounded. In early 1975, BP's credit rating was reduced by an American bank from a triple A to a double A when raising a loan, and one of the reasons given was the possibility of an increase in the state shareholding in BP. Apparently, the company was told that if this threat were removed it would return to a triple A rating.<sup>3</sup>

In this context the claims frequently made by Mr. Benn and other Labour MPs that the Conservative Party's opposition to changing the licence terms was merely a defence of oil companies' interests totally misses the mark. It was, as they themselves admitted, based

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1. The Economist, 'Who does best out of America's 43% of North Sea Oil', September 24, 1977.

2. Cit. in 891 H.C. Deb. col.505 (April 30, 1975).

3. 891 H.C. Deb. col.535 (April 30, 1975).



on a general concern for the interests of all transnationally operating British companies and financial institutions.<sup>1</sup>

The Labour Government's decision to incorporate all the new regulations into the Act and to hold informal consultations with the licensees throughout 1975 provided a means of overcoming the obstacles which the previous Government had perhaps recognised and thought insurmountable. The consequence was that the revision of licence terms was not done unilaterally (other than in the most formal sense). Lengthy negotiations between the Government and the UKOOA took place in the Department of Energy and undoubtedly persuaded the Government to table a large number of amendments to its proposals in Parliament, not least the rewritten model clause on depletion rates.

In addition, the Government asked Parliament to legislate in detail, instead of seeking from it a broad delegation of power. The entire body of regulations, new and old, were contained in model clauses in Schedules to the Bill, which was to be debated at a time when the Government had considerable difficulties in obtaining a majority. The substantial modifications to the original proposals which resulted testify less to the success of the Parliamentary Opposition than to the Government's desire to produce a compromise satisfactory to the oil companies. Their success in doing so allowed one deputy secretary at the Department

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1. See, for example, remarks made in H.C. Deb. Standing Committee D, cols.1158-63 (July 3, 1975); 891 H.C. Deb. cols.494-511 (April 30, 1975); 364 H.L. Deb. cols.548-62 (September 25, 1975); 365 H.L. Deb. cols.1765-66 (November 11, 1975).

of Energy to announce with evident pride that most oil companies

...recognise that they are kept in touch and consulted to a greater extent in this country by the Government than elsewhere in the world. They know our doors are always open.<sup>1</sup>

The result was, however, much more than the modification of certain key regulatory provisions. As a consequence of the procedure adopted, considerable obstacles were placed in the path of any future amendment of licence terms. The whole of the economic regulation of petroleum production (excluding taxation) is now contained in the licences, but they are treated as if they are 'wholly similar' to private contracts, with a formal specification of rights and duties.<sup>2</sup> Further legislation is therefore required before their terms can be altered. Since there is still no re-negotiation clause, the terms of licences once allocated can be varied only at the cost of a repetition of the Government's action in 1975; i.e. a new Act is required. Relative to most other oil-producing states, the petroleum licensee thus received a considerable degree of legal security in the United Kingdom.

Finally, it should be noted that the negotiations concealed some rather brutal economic facts. Firstly, the Government was highly dependent upon the ability of both oil companies and international banks to advance the additional capital required for the development of several fields which had been recently discovered

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1. John Liverman, reported in The Scotsman, 'Government's record defended', July 27, 1976.

2. T.C. Daintith and I. Gault, 'Pacta Sunt Servanda', op.cit., p.42.



and which were known to contain recoverable reserves in sufficient quantity as to justify their development. When that capital did not seem to be forthcoming in 1975, the objective of self-sufficiency by 1980 seemed in jeopardy, and strengthened critics' arguments that the Government's proposals were undermining the 'confidence' of investors. This certainly influenced the course of the negotiations, as it may have been intended to. Secondly, the Government's economic forecasts were highly dependent upon information supplied by the oil companies themselves. It seems quite possible that this had a decisive influence upon the Government's actions in 1974-5. In 1975, official estimates were that North Sea oil production would reach 20 million tons in 1976, rising to 100 million tons by 1978.<sup>1</sup>

However, an American publication called 'The Oil and Gas Journal' conducted its own study of North Sea prospects and produced estimates which differed substantially from those of the Department of Energy.<sup>2</sup> According to the American figures, production from the UK fields was expected to reach 42 million tons by the beginning of 1977, compared with the Department's figure of 30 million tons. The Journal's figures were based on lengthy talks with the principal oil companies involved in production work. The Department's estimates of future production

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1. Department of Energy, Development of the oil and gas reserves of the United Kingdom (1975).

2. The following is based on a report in The Guardian, 'Which are we to believe?' July 3, 1975.

levels were based upon information supplied by the oil companies.

At the time one writer commented that

If the companies are more optimistic than they were about the problems being overcome and leading to a faster flow rate, then it does cast a doubt over companies' continuing assertions that many of the North Sea fields will not be developed because of punitive measures by the Government.<sup>1</sup>

The Department's low figures may have encouraged the Government in the view that further investment was essential if self-sufficiency was to be reached by 1980. They certainly emphasised the continuing importance of the major oil companies and international banks for the development of North Sea oil.

Throughout this period in which the licence terms were amended, the Government strove to present a particular image of itself and its actions: it was extending public control over an essential national resource, remedying the neglect and mismanagement of the preceding Government. This was not mere political rhetoric, but rather the presentation of an image which fulfilled an important legitimating function at a time when many people regarded the legal arrangements between state and oil companies as much too favourable to the companies. It was also an image which made the legal

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1. loc.cit.



aspects of the action seem less exceptional. However, it had the further effect of exaggerating the element of change in the position of the licensees after the Government's 'remedial' action. In this chapter I have attempted to show how little that position was affected and to explain why this was so. In the next chapter I examine the more serious threat to the licensees' interests presented by the Government's attempt to secure physical possession of the fruits of the licence: the produced oil.

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CHAPTER FOUR

The Introduction of Majority State Participation



**Contents:**

1. The problem of legality
2. 'Voluntary' negotiations.
3. The question of ownership
4. The participation agreements
5. The establishment of ENOC

There has been too much talk of expropriation, nationalization, confiscation, just compensation, and the like, without considering the economic issues. The parties are negotiating about profits, and ownership is only the right to future profits.

M.A. Adelman<sup>1</sup>

In this chapter I examine a second aspect of the 'crisis of legality' which arose in 1974 with respect to proprietary arrangements for North Sea oil development: the Government's decision to introduce majority state participation into current (i.e. pre-1974) petroleum licences for commercial oilfields. To what extent did majority state participation diminish the economic control of those companies already holding licences?

I argue that majority state participation, through the BNOC, has had no significant effect on the dominance of American and British oil companies in the North Sea. It does not preclude a considerable degree of economic control being vested in the private companies. For example, with respect to pre-1974 licences, the key powers over extraction and disposition of oil remained in private hands, and company profitability was not adversely affected.<sup>2</sup> Nonetheless, the Labour Government's assertion that it intended to substantially modify licence rights created a 'crisis of legality': the companies holding petroleum production licences had assumed their licence rights would be protected and guaranteed

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1. The World Petroleum Market, p.212.

2. Throughout this chapter I consider only petroleum licences which were current at the time when majority state participation was introduced, i.e. those allocated before 1974.



by the state but were confronted with a Government which had publicly declared that it had no intention of doing so. The focus of this chapter is upon the resolution of that crisis: that is, the ways in which the Government obtained greater 'public control', but not at the expense of private control of key aspects of production and distribution.

#### 1. The Problem of Legality

Like the unilateral decision to revise the terms of production licences, the proposal to introduce majority state participation into existing licences in 1974 was a most unusual one. The Government had declared its intention to take a majority holding in licences awarded on terms that anticipated no such transfer to the state.<sup>1</sup> While it was incontestably the case that any British Parliament could do this by exercising its sovereign power, it has not been the practice of British Governments to ask Parliament to act in such a manner, particularly with respect to legal arrangements which are contractual in character.<sup>2</sup> An expectation is therefore established that the Crown will respect its legal obligations and act 'in good faith'.<sup>3</sup> Since the licences were (and are) contractual in character, this attempt to take a 51% state share of the 'fruits' of the labour carried out under

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1. White Paper, p.5.

2. See chapter three, s.1.

3. The influence of this idea can be seen in the justification advanced by the Department of Trade and Industry for going ahead with the discretionary award of licences at the time of the fourth round in spite of the results of the auction experiment: see chapter two, s.4.

these licences, raised the question of how secure other public contracts were. From the Government's point of view, it was essential to reconcile the sovereign character of its action, an unusual one in the United Kingdom, with its claim to respect the Rule of Law, or more precisely, with its desire to encourage further investment by private companies in offshore oil development.

Underlying this problem of legality were specific economic considerations. In particular, it was commonly assumed that 51% state participation meant that 51% of the future profits from commercial fields would be transferred to the Government.<sup>1</sup> While there was no legal barrier to such a transfer, the Government, by dint of international law obligations, would have to pay compensation. Such a course would have involved payment of enormous sums to the licensees. How would the Government find the money to make such payments?

The Government set out its proposals in a White Paper in July, 1974.<sup>2</sup> To start with, it distinguished 'future' from 'existing' licences.<sup>3</sup> It was to be made a condition of future licences that the licensees should, if the Government required it, grant majority participation to the state in all fields discovered under those

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1. Apparently, 'most observers were expecting participation ... to be enacted by legislation with suitable proposals for compensation to go along with it': Petroleum Times, July 26, 1974 at p.45.

2. White Paper, op.cit.

3. op.cit., p.5.



licences. Such participation would follow the 'carried interest' pattern developed in Norway, which gives the state the option to acquire ownership of a specified proportion of oil or profits, if it meets the same proportion of costs.<sup>1</sup> Since the Government was constrained from introducing such new conditions only by their possible failure to attract bids for new blocks, this proposal was not especially controversial: it was their apparent intention to introduce majority state participation into 'existing' licences for commercial fields that provoked controversy, and raised questions of legality. However, the choice of words here is highly significant. The Government began by stating its belief that majority state participation in the 'existing' licences for commercial fields provided the best means for 'the nation' to benefit from the oil discoveries. Since the Government would contribute its share of costs, including past costs, there would be no unfairness to the licensees. It pointed out that this sort of arrangement was not unusual: it had been adopted with the consent of the oil companies in virtually all the major oil and gas producing states. In addition, public sector participation via the National Coal Board and British Gas had already worked successfully 'without injury to oil company interests'. It continued:

The Government hopes that the companies will recognize the strength of their views on this. They want the oil companies to continue to invest in the North Sea on

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1. In the event, 'carried interest' was dropped as a condition in the fifth and sixth rounds, due to objections from the oil industry. This form of state participation was, incidentally, favoured by the then Leader of the Opposition, Mr. Edward Heath: see 871 H.C. Deb. (March 26, 1974), col.339.

profitable terms. They will be very ready to listen to what the companies say and consider with them how the common interest can best be served. They are sure the industry will want to submit their views at the earliest possible moment and to enter into talks on this basis. The Government will be inviting them to do so shortly.<sup>1</sup>

From this passage it is clear that the Government were uncertain about what to do, but whatever they did, they would only do as a result of negotiations with the companies. Any hint of coercion by the state was avoided, and a picture of 'reasonableness' presented.

It is important to note this uncertainty on the part of the Government if we are to understand subsequent developments. Neglect of this has led at least one writer to assume a linear development in the establishment of majority state participation which simply was not there.<sup>2</sup> Tensions and contradictions not only characterised the process but also were not entirely resolved in the final legal forms of state participation. At this stage there were few definite features in the participation policy: the Government was seeking a majority holding, and wished to obtain it through 'talks' with the oil companies. It intended to hold the interests acquired through a national oil company, which would eventually participate in all stages of the production and distribution of oil, competing with the private oil companies. The British National Oil Corporation (BNOC) would represent the Government in the present

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1. White Paper, p.5.

2. J.C. Woodliffe, op.cit. Harold Wilson has since claimed that the Labour Party had not worked out its oil policy before the February Election and that it took 'four months before any clear statement of policy could be made': Final Term, p.41.



consortia and build up a supervisory staff that would allow it to take this active part in future offshore oil development.

After the publication of the White Paper, there were no positive steps taken to develop these features of majority state participation until late November 1974. Indeed, the Government's approach to the three branches of its new oil policy: taxation, licence controls, and participation, suggests some scepticism on its part about the very objective of majority state participation. Discussions between the Government and the oil companies about the various proposals did not begin simultaneously. As early as September 1974, the Government had set out the basis for its reform of taxation and licensing controls, sending outlines of proposals to all companies with North Sea interests.<sup>1</sup> However, participation was left undefined at that stage. Even by October, the Government had not set out the basis on which it would take 51% participation. In fact, discussions between the Government and oil companies did not begin until late November. It might be argued that failure to tackle all three aspects of its policy at once left the Government with very little bargaining power over the introduction of participation. The Government could not have been unaware of this possibility when they ordered their priorities.

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 1. See The Financial Times, 'Killing industry faith in Government fairness', September 20, 1974.

There were several reasons for its hesitation over the question of participation. Firstly, a political one arising from the probability of another General Election in the autumn. Secondly, the oil companies made their opposition to the proposal very clear. Finally, there was a contradiction between the Government's desire to obtain majority state participation in pre-1974 licences and its wish to encourage further investment in offshore oil development.

The taking of any firm decision on an extension of public ownership seemed to be precluded by the likelihood of a second General Election in 1974. In the course of the autumn election campaign, further statements were made by the Labour Party on oil policy, contained principally in its Election Manifesto.<sup>1</sup> They stressed the key role of the North Sea oil discoveries for the Government's economic programme.<sup>2</sup> This made necessary a degree of 'public control in the interests of the whole community', which included the taking of majority state participation in all future oil licences, and negotiations with holders of pre-1974 licences in commercial fields with a view to securing a majority state share of their interests.<sup>3</sup> The Manifesto reaffirmed Labour's intention to establish a British National Oil Corporation through which the Government would exercise its participation rights. It would play an active role in the future development, exploration,

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1. Labour Party General Election Manifesto, October 1974, pp.11-12.

2. loc.cit. This was merely one expression of the Labour Party's general economic policy, which envisaged a greater role for the state as a pre-requisite for economic growth and full employment.

3. op.cit., p.11; and also for the following sentences.



and exploitation of offshore oil.

The second reason for delay was the opposition which the Government encountered from the oil companies themselves to the idea of majority state participation. Immediately following publication of the White Paper they made their dissatisfaction known. The first company to criticise the idea, Shell, claimed it would slow down oil development.<sup>1</sup> Apparently this view was shared by the National Coal Board (NCB) which also had licence rights in the North Sea.<sup>2</sup> BP issued a letter to its staff stating that the official proposals seemed 'likely to lessen confidence generally, and to reduce incentive to explore and develop off the UK'.<sup>3</sup> Burmah followed a similar procedure, setting out its opposition in a letter to its staff.<sup>4</sup> In addition, the press reported the 'anxieties' of various oil company executives.<sup>5</sup>

Their principal objection seemed to be this: if the Government attempted to take a majority share in licences for all commercial fields, then a climate of 'uncertainty' would be created in which further investment would be impossible. In other words, they would not advance the capital necessary to develop various fields which were known to contain large quantities of oil.

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1. The Financial Times, 'Oil Companies' campaign against State plans', July 27, 1974.

2. loc.cit. The NCB's interests were taken over by the BNOC.

3. loc.cit.

4. loc.cit.

5. For example, the remarks made by the Chairman of Berry Wiggins, one of the largest British-based oil concerns, reported in The Financial Times, 'National Oil Company plans attacked', September 20, 1974.

Nonetheless, opposition was expressed in a discreet manner at this stage. The letters to staff were private documents, and were not intended as contributions to a public debate. The companies had no wish to align themselves too closely with any particular party when another General Election was expected in the near future. It was only after the October Election that opposition from the oil industry became intense.

Finally, there seemed to be a basic contradiction between the Government's desire to obtain a majority state share in current licences and its claim that majority state participation would not be incompatible with the oil companies' interests.<sup>1</sup> If this was to be achieved, state 'ownership' would have to be divorced from the power to extract and to dispose of the oil. If that could be achieved, what purpose would state participation serve, if any?

The problem was not only one of 'squaring the circle' but of finding a means by which a solution could be reached. The solution to the problem of procedure was anticipated in the White Paper: there would be a series of negotiations between the Government and the oil companies. This procedure had several advantages over legislation: firstly, if the negotiations were voluntary in character (and successful), payment of compensation could be avoided; secondly, it minimised the possibility of retaliatory action against British companies operating abroad;<sup>2</sup> thirdly, it lent support to

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1. Particularly when the Government's claim was reiterated in the uncompromising form given to it by Harold Lever in early 1975.
  2. In particular from the US Government for any action damaging the interests of the many US companies operating in the North Sea.



the claim that the Government was acting 'in good faith', and perhaps prevent a loss of further investment in oil development; finally, it cast the state in the role of one 'party' to a bargaining process, obscuring the fact that the subject of 51% state participation was only put on the agenda as the result of the state's exercise of sovereign power.

For all these reasons, majority state ownership seemed best able to be achieved through negotiations between the Government and the licensees, represented by their operators, the oil companies. However, for any of the advantages to be gained, the negotiations had to be voluntarily entered into. This was essential if the state was to be presented as a party to a bargaining process, distinguished from the other parties only by its 'possession' of sovereign power with which to bargain.

## 2. 'Voluntary' negotiations

While the participation proposals were not given top priority, it would be wrong to conclude that the Government did not consider them particularly 'sensitive'. So important were the negotiations considered that they were taken out of the jurisdiction of the Department of Energy and given to a negotiating committee, specially created to negotiate with the licensees. The committee consisted of Mr. Edmund Dell, representing the Treasury, Lord Balogh, Minister of State in the Department of Energy, and was chaired by Mr. Harold Lever, a non-departmental Cabinet Minister,<sup>1</sup>

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1. His title was that of Chancellor of the Duchy of Lancaster.

who was obliged to report to Mr. Varley, the Energy Secretary.<sup>1</sup> All these men had considerable knowledge of North Sea developments. Both Mr. Dell and Mr. Lever had been members of the Public Accounts Committee in 1973 when it produced its controversial report on North Sea oil and gas, which severely criticised the policies of successive British Governments.<sup>2</sup> Lord Balogh had also been a critic of past Government policies, having voiced his criticisms as early as 1971.<sup>3</sup>

A series of 'talks' with the oil companies on participation was begun in late November, 1974. A letter was sent to all licensee companies in oilfields so far declared commercial, inviting them to enter into negotiations.<sup>4</sup> However, it was couched in the most general form of an invitation only, and did not therefore suggest that the Government had any detailed conception of state participation to discuss. It merely wished to ascertain the views of licensees on its proposals. The majority of licensees replied to the invitation, a fact which the Secretary of State interpreted to mean that 'most of them are seriously considering the question of participation'.<sup>5</sup>

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1. Apparently, some of the later talks took place with separate members of the negotiating team, and even with senior officials of the Department of Energy: see The Financial Times, 'Seeking one industry voice on PRT', January 10, 1975.

2. See chapter two, s.4.

3. loc.cit.

4. 882 H.C. Deb., cols.14-15 (November 25, 1974).

5. loc.cit., at col.15.



Since majority state participation would have different effects according to a field's peculiar characteristics, the negotiating team met the oil companies individually and not in groups.<sup>1</sup> In these negotiations with the Government as in the others, each licensee was represented by its operator, always an oil company and usually one of the 'majors'. While the licensee and the operator may be one and the same, the norm in the North Sea is for licences to be held by consortia, participating in joint venture arrangements.<sup>2</sup> It is the operator then, who assumes the responsibility of seeing that the work of extraction is done, and who usually represents the consortium in any major negotiations with the Government.

The first companies to 'talk' with the negotiating team were those oil companies with the largest interests in the North Sea: BP, Shell, and Esso. These talks were held on November 28th and 29th, and, like all the talks, and the subsequent negotiations, they took place in private.<sup>3</sup> The choice of these companies to head the list was hardly surprising, since together they controlled the greatest share of oil reserves yet found in the North Sea. However, the choice of the Gulf Oil Company to follow them was less obvious, since Gulf was not even an operator in its partnership with Conoco and the NCB. Its choice as the first of

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1. The Financial Times, 'Seeking one industry voice on PRT', January 10, 1975.
  2. For an explanation of this, see chapter one, and also chapter two, s.3.
  3. The Financial Times, 'Participation: getting down to the nitty-gritty at last', November 29, 1974. The next few paragraphs draw on the account given in this article. The fact that the talks were held in private did not prevent the appearance of apparently well-informed reports in the press, especially in The Financial Times.

the remaining companies may have been determined by its vocal opposition to the Government's proposals, and its threats to withdraw completely from the North Sea.<sup>1</sup>

It is important to stress the preliminary character of these talks between the oil companies and the negotiating committee. They were designed to highlight the main problems before serious negotiations actually began. They did not represent a willingness on the part of the companies to negotiate about majority state participation in existing licences, still less their acceptance of it in principle. Indeed, Shell and Esso proved highly resistant to the proposal until mid-1976.

The obstacles to an agreement were now clearly visible, and they were considerable. Firstly, it was not at all clear what participation was specifically designed to achieve. Mr. Lever had enunciated a 'no loss, no gain' principle, whereby acceptance of a majority state share would leave the companies' profitability from oil production unchanged. In other words, profits would still be the same under 49% private control as they would have been under 100% control by the oil companies of produced oil. In addition, the Government assured the oil companies that they would be able to buy back the state's share of crude oil output for 'several years'.<sup>2</sup> This made 'majority state participation'

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1. This is suggested in the above article.

2. 'Seeking one industry voice on PRT', op.cit.



a largely cosmetic exercise from the outset. However, Mr. Lever proudly declared that he did not even know what form that cosmetic exercise would take!<sup>1</sup> Secondly, the manner in which the Government proposed to obtain majority state participation - through 'voluntary' negotiations - seemed to contradict the objective implied by majority participation on any definition. After all, why should licensees voluntarily surrender the largest share of profitable fields? Even if the Government were to offer massive compensation payments in return for a 51% controlling interest in their licences, some companies might simply not be interested. One oil executive, the chairman of Exxon, re<sup>in</sup>arked that, if negotiations were voluntary, his company were not volunteering.<sup>2</sup>

The choice of method, voluntary negotiations instead of legislation, is easy enough to explain. Negotiations on a voluntary basis presented a picture of fairness and avoided any hint of nationalisation. This was important for two reasons: firstly, it reduced the possibility of a confrontation with the United States, whose companies constituted the majority of foreign companies operating on the UK Continental Shelf; secondly, it reduced the risk of repercussions against BP, at that time 48% owned by the Government, and with important interests in the already volatile Middle East.<sup>3</sup> Nonetheless, there was a constant tension between the

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1. loc.cit. It was up to the oil companies to make suggestions.

2. Clifton Garvin, reported in The Times, February 3, 1976: 'Exxon chairman says group not volunteering for state participation'.

3. Cf. Dem, op.cit., pp.106-7.

Government's claim that its acquisition of a majority state share in current licences would result from negotiations, and the language of sovereign power sometimes used by its spokesmen. For example, Mr. Benn commented on the Government's 'determination' to acquire a majority stake, provoking such an uproar among his fellow MPs that an assurance was hurriedly given by the Government that the negotiations were indeed still 'voluntary'.<sup>1</sup> As I shall show in the next section, a small element of coercion was, however, not excluded from the Government's means of persuasion.

Once the Government had decided to eschew compulsion and proceed by means of voluntary negotiation, it could only secure a majority stake in the licences by making a highly attractive offer to the companies. The negotiations over the next two years are the history of their attempts to do this. The only means of persuasion the Government had at its disposal were:

(1) use of regulatory controls over assignments (a company could only sell its interest in a licence if it agreed to a majority state share); (2) bribery, by offering favourable treatment in the next round of licensing. Unfortunately, the most promising areas of the North Sea had already been licensed and unlicensed blocks were not likely to prove sufficiently attractive to companies to encourage them to surrender a 51% share in their

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1. 905 H.C. (Oral Answer) (February 16, 1976), at col.921. He said: 'We have made it clear in the participation which we are determined to get with all the oil companies in the North Sea', but was interrupted before he could finish the sentence.



proven reserves; (3) provision of guarantees for borrowing.

After these talks were completed in early January, the Government awaited a response from the oil companies. In so far as any response was forthcoming in 1975 it was not favourable. Both Shell and Esso, who together controlled about one half of the fields under development, refused to participate in any further negotiations until mid-1976. Other companies did enter into further discussions but no progress was made, in spite of the reiteration of the 'no loss, no gain' principle by Mr. Lever. Government spokesmen went to great lengths to reassure the companies, especially at the time of the Petroleum and Submarine Pipe-Lines Bill's passage through Parliament. For example, Lord Balogh insisted in July that

... participation is not the same as nationalisation. I cannot stress that too often: it is participation (sic!). I repeat that participation is a means of partnership between the Government and the oil companies. Our objective is to obtain by negotiation 51% participation in commercial fields regulated by current licences.<sup>1</sup>

Indeed, under Mr. Lever's tutelage, the language of 'partnership' quickly substituted itself for the language of state power so evident in the first Manifesto of February 1974.

An interesting feature of these early discussions was the difference in style between American and British oil companies. The first American negotiators were described by a former Department of Energy official as 'the mirrors and beads boys',<sup>2</sup>

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1. 363 H.L. Deb. (July 23, 1975) at col.330.

2. Seminar on the negotiation of participation agreements between ENOC and the private oil companies, held at the Centre for Petroleum and Mineral Studies at the University of Dundee, April, 1979.

which says a great deal about their attitude to the Government's demands.

In general, the American response was noisier and more aggressive. Crude threats were made as well as apocalyptic forecasts of the effects of the participation policy. For example, the chairman of Allied Chemicals, a former Secretary of Commerce in the US Government, warned the British Government that it risked losing hundreds of millions of dollars of American investment if it persisted with its participation policy in its present form.<sup>1</sup> For the Government

... to come in at a late stage and apply this policy to successful oilfields raises some question as to how much investment we can put into chemicals and petrochemicals in the future.<sup>2</sup>

This bullish approach received little support from the American Government which was more concerned with the apparently weak state of British capitalism as a whole. Reports of imminent collapse appeared regularly in the American press at that time.

By the end of 1975 the negotiating committee was still not able to report any significant success in its attempts to secure majority state participation by voluntary negotiation with licensee companies. Seven months after preliminary talks had begun, Mr. Lever announced that four oil companies had agreed in principle

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1. Allied Chemicals has interests in the Claymore and the Piper fields. The chairman, Mr. Connor, was a member of a delegation of US businessmen invited by Mr. Healey to look at the 'British economy' at first hand, in an attempt to counter highly pessimistic reports then current in the United States: see report in The Scotsman, September 22, 1975: 'US North Sea oil warning'.
2. loc.cit.; see also The Financial Times, September 26, 1975, 'What the presidents saw'. According to this report, the delegation of American businessmen of which Mr. Connor was a member was unanimous in condemning the Government's policy on state participation.



to 51% state participation in their North Sea oilfields.<sup>1</sup> However, the companies concerned, Burmah, Deminex, Tricentrol, and Blackfriars Oil, were all minor ones and were vulnerable to Government pressures because of their financial difficulties. So far as the other companies were concerned, it was merely stated that 'constructive discussions' were taking place with a large number of companies, representing half the interests in the North Sea.<sup>2</sup> However, by December, only another four small companies had reached agreement in principle with the Government.

It was not until the banks raised questions about title to the oil in the course of negotiations with the Department of Energy that the Government glimpsed a way of obtaining its 51% stake in commercial oilfields without damaging the interests of the private companies concerned.

### 3. The Question of Ownership

Before the Labour Government expressed an interest in the ownership and control of North Sea oil, the banks had already identified this as a key problem, albeit for rather different reasons.

The large sums involved in developing oilfields in the North Sea led many companies to seek funds from the banks. This did not apply to the majors who financed field development from their own funds but it did involve a number of other large

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1. 894 H.C. (Oral Answer), (June 25, 1975), col.445. BP was also reported to be nearing acceptance.

2. loc.cit.

companies to such an extent that, by May 1977, the banks had provided about £5 billion for the development of North Sea oilfields.<sup>1</sup> Before lending such large sums they looked very carefully at the security for their loans. They had to ensure that in case of failure they could control the extraction of oil. Any such arrangement had to be cleared with the Department of Energy which had ultimate discretion over the tenure of petroleum licences.

When the banks first looked at the question of security they discovered one cardinal fact about oil resources in the United Kingdom: the state owned the asset on which finance was to be secured. In this respect the UK environment differs from the United States, where most of the oil (at least until the Proudhoe Bay discoveries) was to be found on private land, and where operators had a right to the oil in the ground, usually through a leasing arrangement. Since the banks concerned were either big American banks like Chase Manhattan, Morgan Guaranty, Citibank and Texas banks or British banks like Barclays entering into oil financing for the first time, the American experience in oil financing provided the prism through which the banks viewed North Sea development. The state's ownership of oil thus presented a problem, albeit one which was quickly resolved.

It was quickly appreciated that ownership of the oil in the ground is of no value unless it is capable of being extracted and

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1. The Banker, May 1977: 'Financing takes new forms', p.75.



marketed and the owner or licensee has the right to do so. As one lawyer commented in a seminar specially concerned with this question,

It is this right to extract and market the oil on a continuing basis which lies at the heart of the question of security, and not any question of title to it as it lies in the ground.<sup>1</sup>

Apparently, the constitution of a security would be simple were the borrower the sole licensee. The fact that the borrower would in most cases be one of several joint licensees complicated matters. How the bankers and their hired lawyers resolved questions of security need not concern us here. It is sufficient to note that they drew the attention of the participation negotiators to one salient feature of North Sea oil development: the Operating Agreement and its consequences.

When a licence is granted to a consortium, the licensees collectively have the right to extract oil from the licensed area. It is their custom to make a separate agreement, called an Operating Agreement, which will specify their respective shares, the manner in which the licensed area will be exploited and the manner in which each licensee will be entitled to appropriate to himself his own share of the oil once produced. The important point here is that, until the point of appropriation, the borrower has no separate title to the oil, but only an undivided interest in common with his co-licensees. One of the licensees

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1. G.D.M. Willoughby, 'Legal Problems in Financing North Sea Oil with Special Reference to Problems of Creating Security', p.4 (paper presented at Law Society Conference on 'North Sea Oil and the Law', held at Worcester College, Oxford, September 1975).

with experience in oil extraction will be appointed the Operator and will carry out the actual operations; the other licensees and especially those with minority interests may, at least in the production stage, have little or nothing to do other than to take their oil at the shore terminal and sell it. Therefore, in the case of one of several licensees the right to appropriate, exercisable by himself, assumes a greater significance than the right to extract, which is exercisable only jointly with the others. Mr. Willoughby identifies this as the key right from the 'lender's point of view'.<sup>1</sup> The Department of Energy negotiators identified it as a key right also, but for very different reasons.

The right to appropriate implied a passive participation by the holder and so suited the embryonic national oil corporation with its small staff. Securing such a right to appropriate 51% of the produced oil, on the condition that ENOC would pay for it at market prices, would 'ensure a title for the British people to the oil itself',<sup>2</sup> but would not affect the beneficial interests of existing licensees, nor the actual process of extraction, nor would it incur any additional expenditure since the original licensees would continue to be responsible for payment of all capital ~~and~~ operating costs, royalties and taxes. ENOC was to hold the Government's share and would become a co-licensee together with existing licensees in every <sup>licence</sup> ~~life~~ comprising a commercial oilfield.

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1. op.cit., p.4.

2. That is, to produced oil: see Lever 886 H.C. (Oral Answer) (February 19, 1975), at col.1339.



Such a procedure has in fact been quite common in the North Sea operations of American oil companies. These companies have often held their licences in a separate company registered in the UK. However, in order to retain certain tax advantages for the parent company, the licensee assigned the benefits of the licence to an American affiliate, subject to the latter company assuming all the costs and obligations as well.<sup>1</sup>

This last feature supplemented the 'no loss, no gain' principle, and, together with a presence for BNOC on the various operating committees, made the British form of state participation unique in the world. In particular, the idea that companies would be no worse nor better off as a result of state participation

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1. Changes in US tax law have made this arrangement less important in recent years. Previously, the US tax laws dictated that for optimum tax treatment all costs had to be incurred by a company incorporated in the USA. Since the Petroleum (Production) Regulations in the UK stipulated (until 1976) that applicants for licences on the UK Continental Shelf had to be persons who were citizens of the UK and colonies resident in the UK or companies incorporated in the UK, there was a potential conflict. The solution adopted involved the use of 'Illustrative Agreements': agreements between a licence-holding UK subsidiary of a US parent company and an affiliate of that company incorporated in the US, but operating through a branch in the UK. It provides that while the UK subsidiary shall remain the licensee for all purposes, the US affiliate shall put up all the funds and equipment for exploration, development and production, and that in consideration for this any petroleum won and saved shall be owned by the US affiliate. The economic interest in the licence is thus 'passed through' from the UK subsidiary to the US affiliate. It is similar to the roles of trustee and beneficiary, with the UK company holding the bare legal title and the US affiliate owning the beneficial interest under the licence. Cf. Adrian D.G. Hill, 'Joint Operating Agreements', paper 14 in Proceedings, vol.I, op.cit., esp. at pp.17-18.

... embodies the essential difference with Government participation as it has been implemented in OPEC countries, where the host Governments took a major financial stake in existing oil concessions.<sup>1</sup>

Once the goal of participation had been redefined as 'a formal assignment of the licence by the companies to themselves and BNOC jointly',<sup>2</sup> giving BNOC a right to appropriate 51% of the produced oil at market prices, the Government expected agreements to be reached with the major oil companies in the near future. As I show in the next section, this did indeed happen. Nonetheless, there was little the Government could have done to force them to conclude agreements.

The use of state power was not entirely absent from the negotiations however. Several of the smaller oil companies found themselves in financial difficulties in 1975 and required additional finance to cover their share of development costs. One means by which this could be done was a 'farm-out' arrangement, which involves assigning an outside party a share in a licence in return for providing development capital. Since all such assignments required approval by the Department of Energy, the Government was given an opportunity to insist on participation. For example, a small British company, Berry Wiggins, assigned one half of its 23% share of a licence for several unexplored blocks to Consolidated Gold Fields in return for the latter company's undertaking to meet some of the exploration costs. However,

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1. Robert D. Vock, 'Government Participation UK Style: Some Legal Aspects', in Proceedings, op.cit., vol.I, Paper 18, at p.2.
2. Dr. Dickson Mabon's words from the second reading stage of the Participation Agreements Bill: 939 H.C. Deb. (November 18, 1977) col.981.



Departmental approval was conditional on acceptance by both companies of the principle of majority state participation in the event of a future commercial discovery.<sup>1</sup>

Other small companies were led to accept the principle of state participation by their need for Government guarantees to raise capital to cover their share of the cost of field development: in Tricentrol's case, its share in the cost of developing the Thistle field (£280m.); in Burmah's case, acceptance of the principle was one of the conditions for the Bank of England's intervention to save the company from liquidation.

However, the exploitation could work both ways. Companies experiencing financial difficulties could use participation as a means of obtaining capital from the Government or guarantees which would then allow them to borrow privately. The state's role in the Thistle field development shows a facilitative rather than a coercive role. As early as autumn 1974, two companies in the consortium, Tricentrol and United Canso, discovered that they lacked the corporate assets necessary to raise funds for the development of Thistle on their own credit. The Government resolved this firstly by providing 'holding' guarantees to the other partners; in other words, it stated that it would meet their share of expenditure if necessary. Secondly, the Department of Energy provided a £38.3m. loan guarantee to support Tricentrol's share of the development cost in exchange for a broad

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1. Dam, Oil Resources, pp.116-118.

participation agreement. Had the state not intervened in this way, the development programme for this field would almost certainly not have gone ahead as rapidly as it did.

The only time when the Government seems to have considered the extensive use of state power in its negotiations was in early 1975. At a Press conference in New York, Mr. Lever claimed that failure to reach widespread agreement to the proposed 51% state participation by voluntary means, could force the Cabinet to consider using statutory powers to reach this goal.<sup>1</sup> However, this 'threat' was clarified in the House of Commons very soon afterwards. Mr. Lever insisted he had made it 'absolutely plain' to the oil companies that the Government would 'scrupulously honour all their contractual and commercial obligations'.<sup>2</sup> He had no statutory powers to compel them if they decided not to participate on the terms outlined. If they did not wish to participate, he added,

... the Cabinet might feel obliged to nationalise that proportion of the licences that it thought right to nationalise ...<sup>3</sup>

with compensation, of course. Indeed, the companies' present assets and future profits were treated with considerable respect in these negotiations at all times. In reply to criticisms from the Left of the Parliamentary Labour Party, the chief negotiator declared that if they wished the negotiations to result in

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1. The Financial Times, 'Lever warns US groups over North Sea oil', February 5, 1975.

2. 886 H.C. Deb. (Oral Answer) (February 19, 1975) cols.1340-1.

3. loc.cit.



acquiring 'the right to compel companies to sell their assets at below cost', then they had the wrong negotiator.<sup>1</sup>

In so far as the Government eschewed the use of political power in the participation negotiations, the appearance of a bargaining process between two 'parties' could be maintained, in spite of the gross differences in their respective economic power and, more importantly, in spite of the intention of the negotiating team, the Government, the Treasury and the Department of Energy (i.e. the State) to re-define its own goal in a manner acceptable to the other parties.

#### 4. The Participation Agreements

The ideological significance of majority state participation was never in doubt. Success was a prerequisite to legitimating the relationship between the British State and the international oil industry in the face of a sceptical public. Mr. Lever emphasised that agreements on participation would enable the Government

... to convince the British people that there is now a visible form of partnership with the oil companies which is fair to both parties.<sup>2</sup>

The existing arrangements were not being re-negotiated in such a way that companies would lose financially, nor was the Government intending to make any compensation payments for negotiation. What

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1. 904 H.C. Deb. (Oral Answer) (February 2, 1976) cols.959-961.
2. In a speech delivered at the Institute of Petroleum's Annual Dinner, reported in the Petroleum Review, March 1976. He also said that the Government sought 'closer partnership with the oil companies' (loc.cit.). This theme of partnership was repeated by Mr. John Smith, Minister of State at the Department of Energy in a speech made to the UK Offshore Operators' Association on March 30, 1976 (my copy).

the companies were being offered, according to Mr. Lever, were agreements which legitimated their economic activities.<sup>1</sup>

Nonetheless, the oil companies were in no hurry to secure this legitimation, and negotiations continued from 1975 to 1977, making it the biggest exercise in commercial negotiations ever undertaken by a British Government, and a remarkable example of government by agreement.

The first agreements to be announced were with the Continental Oil Company (Conoco) and the Gulf Oil Corporation (Gulf) on February 26, 1976.<sup>2</sup> The arrangements affected three oilfields, Thistle, Dunlin, and Statfjord, in which the state already had a share through the NCB. That share was thereby increased from one third to 51%. Although much of the detail remained secret, the broad outlines were made public. They indicated that the BNOC was not to acquire a 51% equity interest in any of the fields under development, but would increase the one third share it had held from January 1, 1976 when the NCB's interest was transferred to it, to 51%. The BNOC would have the option to acquire and to market the crude oil from 51% of the production to which it had title. As for the companies they retained their 33 % working interest: their working obligations, and beneficial interests remained the same, and all three parties had to agree on major decisions. For the first three years after these fields

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1. loc.cit.

2. 906 H.C. (Written Answer) (February 26, 1976) col.301.



began commercial production, the two private companies had the right to all the output: subsequently, the BNOC could exercise an option to acquire 51% of the output, rising to 57% after five years. Once the BNOC decided to take its share of the oil, it would have to pay the companies the full market price to ensure that they incur no financial loss. Significantly, in the light of the state's 'fiscal crisis', the BNOC was not to make any additional contribution to costs. The private companies would continue to be responsible for capital and operating costs arising from the interest assigned to BNOC.

The Government stressed that these arrangements were not a 'blue print for future agreements',<sup>1</sup> and Mr. Lever added that

There is no single standard participation model, because circumstances vary from case to case.<sup>2</sup>

Nonetheless, the seven subsequent agreements signed in 1976 involving thirteen companies, contained similar features.

After the earlier announcements about acceptance of state participation in principle by small or financially weak companies, the first agreements to be actually signed came as a surprise, since they involved two of the largest companies in the North Sea and ones which were American-owned. Given the important role of specifically American interests in North Sea development, and their apparent anxieties over state participation, the fact that an agreement had been reached with these companies was highly significant.

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1. loc.cit., col.303.

2. loc.cit.

The conclusion was quickly drawn by some observers that this arrangement did not remotely resemble the kind of dramatic state control originally expected. Andrew Shonfield, the economist, claimed that

What the Government has secured, through the British National Oil Corporation, is not OWNERSHIP in any sense that the word is generally understood: that is, the power to dispose of the asset as the owner sees fit, and an absolute right to all the profits from it. It has been satisfied, indeed, to establish a privileged position as a BUYER of North Sea oil: it has obtained a first option to purchase 51% of the oil output. And it has got that by guaranteeing to the companies that they will not be worse off by selling the oil to it rather than to anyone else: that is, that they will be paid the market price for it.

A leading firm of stockbrokers went further and claimed that this sort of agreement on majority state participation had shown the term 'participation' to be 'somewhat of a misnomer': the agreements could be better defined as 'option deals'.<sup>2</sup> Neither of the essential elements of participation: a Government option to buy 51% of production at market price, and Government representation in operating committees, would affect the profit interests of the companies concerned. Indeed, another firm of stockbrokers thought so little of the participation agreements that, since profitability was not affected, they did not bother to show the Government as having an interest in those blocks

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1. The Listener, March 18, 1976: 'Enfeebled Government'. He thought the securing of places for Government representatives on the operating boards made no great difference to this conclusion.
2. Wood, Mackenzie & Co., A Summary of UK/Norwegian Offshore Events of 1976, p.2.



where participation had been conceded 'in principle' or otherwise in their diagrams.<sup>1</sup> Professor Dam concluded that 'the White Paper promise of participation was carried out in form rather than substance'.<sup>2</sup>

One important matter was left unsettled after these agreements: what control would BNOC have over the day-to-day operation of the fields in which it had a majority stake? In these cases, BNOC already had a seat on the operating committee (which takes all the vital decisions about the manner in which a field is to be developed) through the former NCB holdings and the negotiating team had agreed not to seek a bigger vote in decision-making than it already had (although, since all major decisions had to be decided unanimously, a greater voting power would not have made any significant difference). However, other companies might be expected to resist any attempt to give BNOC 'a voice and a vote' on the operating committees, and hence the ability to influence the way in which a field should be developed. Indeed, one interpretation of the 'no loss, no gain' principle was that BNOC would have the greatest voting power on the operating committees: a view encouraged by the Government's publicly stated determination to obtain a seat on the operating committees as well as options to the oil.

The formula set out in these agreements was intended to solve the 'participation problem'. At this stage there was growing concern

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1. Scrymgeour Research, The North Sea Oil and Gas Review, 1976, p.9.

2. Oil Resources, p.123.

over the development of several North Sea fields. The investment hiatus which I discussed in chapter three had not yet ended and several fields had reached the development stage, requiring the injection of very large sums of capital. These sums would not be forthcoming unless the international banks and the larger oil companies were 'confident' that their investments would be secure. The real test of this participation formula was whether it would lead to the massive investment required to develop those fields.

Several more participation agreements were reached in the following months (for example, with Tricentrol in March), but it was not until July that the Department of Energy reached its first agreement with an oil major: the British Petroleum Company. Although an acceptance of majority state participation in principle was made by BP as early as April 1975, a preliminary agreement with the Government and BNOC was not concluded until July, 1976, and a final agreement only reached in June 1977. The negotiations were not only lengthy but were punctuated by reports of difficulties and disagreements.

In 1975, BP had agreed to enter into discussions with the Government with a view to agreeing on terms for participation in BP's North Sea oil holdings.<sup>1</sup> However, problems arose in working out the details of the 'no financial loss' assurance, and

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1. 891 H.C. Deb. (April 30, 1975) col.488.



BP sought guarantees over the way in which the Government would exercise its controlling share. Press reports suggested that negotiations had proved difficult, and Sir Eric Drake commented:

We have been having a continual but rather desultory exchange with the Government.<sup>1</sup>

One of the main obstacles was BP's insistence upon a premium price in compensation for the loss of security of oil supplies to its large refining, marketing and chemical activities. While the final agreement did not include such a premium there was a compromise which left the company with jurisdiction over a large part of its crude oil.

The preliminary agreement or Memorandum of Principles concluded in July had three main features:<sup>2</sup>

(1) the Government, through BNOC, would have the option to buy 51% of BP's crude oil from the beginning of 1977.

This was to be a book-keeping arrangement for the first two years. BNOC would sell all the oil taken up back to BP at the same market price.

(2) BP undertook to train several of BNOC's staff in 'downstream' activities (that is, refining and marketing).

This provision distinguished the BP agreement from the others reached at that stage, but there was not to be any direct involvement

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1. Reported in The Financial Times, November 11, 1975: 'Burmah: "State control unlikely"'. Pessimistic reports appeared in The Times (e.g. February 26, 1976: 'Gulf agrees to North Sea share for state'; March 12, 1976: 'Uncertainty over terms slows Forties takeover'; and March 26, 1976: 'Lengthy talks bring success'. In the former report it was claimed that negotiation of a detailed pact with BNOC had 'run into difficulties arising from deeply held objections to the scheme in the upper echelons of the company'.) Indeed, shortly after Mr. Varley had announced to the House of Commons that BP was prepared to enter into discussions (see footnote 1 p.228 ) the chairman publicly denied that any agreement in principle had yet been made: The Guardian, May 2, 1975: 'BP says handover not agreed yet'.

by ENOC in refining and marketing for at least five years. The daily management and the development of the oilfields would remain under private control.

(3) ENOC would have a non-voting presence at BP's main refining and marketing meetings. This would give it an insight into North Sea operations.

To some extent the success of this agreement was undermined by the fact that the Government had a majority shareholding in BP. Suggestions of 'arm-twisting' were common, and were given an impetus by the transfer of 21.6% of BP shares from the Burmah Oil Company to the Bank of England in 1975. According to one report,

BP refuted suggestions that the possible dispersal of the Bank of England shares has been used as a negotiating point in talks about North Sea participation. Nevertheless, it is understood that the two issues have become related, to some extent.<sup>1</sup>

The ambiguous legal status of BP partly undermined the impact of this agreement on the remaining companies which had expressed resistance to the idea. The success of the Government's redefinition of 'majority state participation' would ultimately be measured by its acceptance by these companies, and by Shell and Esso in particular. The two companies operated jointly in four of the fields which were at that time commercial: Auk, Cormorant, Brent and Dunlin. The Brent field was the biggest field yet discovered in the North Sea with two billion barrels of recoverable

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1. The Financial Times, November 25, 1975: 'Burmah: "State control unlikely"'.  
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oil reserves. Together Shell and Esso were the biggest operators in the North Sea with an estimated investment of £4,500m. in the North Sea by the end of 1980.<sup>1</sup>

However, in December 1976 both companies accepted a version of the 'option to buy' offer, when it was supplemented by an assurance that the oil would be sold back to the companies for use in their refineries. In return, the Government secured a right of supervision over the whole of each consortium's oil flows, and not merely 51%. BNOC would have access to just over 45% of the total oil production by 1980.

As a prelude to a legally binding agreement, Memoranda of Principles were agreed between the parties.<sup>2</sup> They had the following features: BNOC would be a joint licence holder with Shell and Esso in all present and future 'commercial' oilfields found under existing licences; the corporation would have the right to participate in the decision-making process for field development: it would be represented on the operating committees and could vote on decisions, but could not veto them; BNOC staff would receive training in crude oil supply, transportation and refining operations.

The key feature was the Government's promise to sell the oil back to the companies if they needed it to meet demand in the British market. Since the two companies would certainly need the

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1. The Scotsman, January 18, 1978: 'Largest single investment in North Sea oil'.

2. See the Department of Energy, Participation Arrangement<sup>s</sup> between Her Majesty's Government, the British National Oil Corporation and Esso Petroleum Co. Ltd.'s Memorandum of Principles, January 5, 1977. (Each memorandum was virtually identical.) These principles were embodied in participation agreements concluded on November 21, 1977: the Department of Energy, Shell/Esso: Participation Agreements: Summary, November 21, 1977.

oil to feed their large refining and marketing operations in Britain, the Government's control was likely to be very temporary indeed. In addition, a number of other features suggested that this form of agreement had the character of a planning agreement: for example, the companies were to inform the Department of Energy of production levels, refinery throughput and output, pricing policies and investment plans.<sup>1</sup>

The success of Shell and Esso in protecting their interests had been considerable. While the Government did obtain certain rights over their oilfields, the precise value of these rights was not easy to ascertain, given the duties also imposed upon it with respect to the exercise of those rights. From the outset, the companies had assumed an uncompromising stance in their negotiations with the Government. After an initial refusal to volunteer for any negotiations at all, they only began to do so when it had become clear that the Government had modified its offer. The agreements were only concluded after six months of hard bargaining during which they refused to compromise on their principal objective: to retain control over all the oil they expected to produce from UK offshore fields, which they planned to use as feedstock for their large refining and marketing operations. Without an assurance that they would retain such control, it would have been extremely difficult, if not impossible, to reach a voluntary agreement on participation.

The oil companies were far from reserved in their reaction to the arrangement. The chief executive of Shell's UK subsidiary sent a message to the company's 16,000 employees explaining how the

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1. Summary, op.cit.



new concept of participation plus the assurance that companies would be no worse off financially gave full protection to the interests of both employees and shareholders.<sup>1</sup> In it, he claimed that this modification of the original concept, was due to the company's strong opposition to the Government's attempt to buy a 51% controlling interest in their North Sea assets. Interestingly, the company chairman was reported as saying that the public relations aspect of participation was one of the most cogent reasons for accepting the deal in principle.<sup>2</sup> He also expressed support for a greater exchange of information between oil companies and the Government. The protection of company interests by this participation agreement was a theme echoed by the chairman of Esso Petroleum.<sup>3</sup>

Further agreements followed swiftly. American oil companies like Texaco and Mobil, which had proved so fierce in their opposition to participation, reached agreement with the Government negotiators shortly afterwards.<sup>4</sup> These agreements were modelled on those reached between Shell, Esso and the Government. Like Shell and Esso, both Mobil and Texaco had large

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1. The Financial Times, January 6, 1977: 'Shell and Esso win right to sell North Sea oil'.

2. loc.cit.

3. loc.cit.

4. 924 H.C. Deb. (January 25, 1977) col.503 (Texaco); 924 H.C. Deb. (January 25, 1977) col.504 (Mobil). An agreement with Chevron, another US major, was reached at about the same time as the one with Shell and Esso: 923 H.C. Deb. (December 21, 1976) col.123.

refining and marketing operations in the UK, but the agreements assured them that their North Sea oil supplies would be available for their refineries: they could buy back from ENOC as much participation crude oil as they could prove was necessary to support their UK refinery operations.

While there were minor differences in the various agreements<sup>1</sup> they all articulated the 'option to buy' principle, and gave ENOC the right to information and a power to vote on, but not veto, the making of decisions.

In retrospect, the decisive stage in introducing majority state participation occurred in early 1976 when the definition of such participation as little more than an 'option to buy' agreement was enunciated. Of course, protracted negotiations did take place after the Gulf/Conoco agreement, but these were largely about the particular form that participation would take with respect to the very diverse interests of the companies concerned. Companies like Gulf and Conoco which did not have the substantial 'downstream' operations of Esso and Shell found it relatively easy to reach a participation agreement in the 'option to buy' form. The sale-back provision in the Shell/Esso agreements has to be seen in this light rather than as an example of the power of 'big multinationals' over a 'weak' Government.

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1. For example, where agreements were signed with oil companies wishing to start up refining operations in Britain in the future, like Amerada Hess and Texas Eastern, the ENOC gave an undertaking to sell them back enough oil for their refineries in the UK. This was hardly an inconvenience since the companies would probably wish to utilise their newly-built capacity in the UK for this very purpose. Since consumption of oil in Britain is very high, a requirement to refine large quantities of crude oil there was hardly an imposition: much oil would be sold as a matter of course to their UK marketing subsidiaries. Nonetheless, the companies did lose the ability to sell any surplus oil on the 'spot' market where they might have obtained a premium on the current market price.



Two other developments lend support to this view: firstly, the changes in the personnel of the negotiating team and secondly, the end of the investment hiatus in 1976. Shortly after the first participation agreements were concluded, Mr. Tony Benn replaced Harold Lever as head of the ministerial negotiating team. The main lines on which participation would be negotiated were by this time well established. Other changes at this time included the replacement of Mr. John Smith by Dr. Dickson Mabon as Minister of State at the Department of Energy. Mr. Smith had had the responsibility of 'steering' the Petroleum and Submarine Pipe-Lines Act through its parliamentary stages. Another member of the negotiating team, Mr. Edmund Dell, who had been a principal member of the Public Accounts Committee when it investigated North Sea developments, was replaced by Mr. Joel Barnett, Chief Secretary to the Treasury. Finally, Lord Barton became a member of the negotiating team.

These changes also reflected the growing control of the Department of Energy over the negotiations. Once the contradictions were removed from the Government policy, negotiating participation became more and more an administrative, as distinct from a political, matter. The bureaucratic mentality defined an 'active' role for the state in terms of the acquisition of information and expertise, and so long as this did not require the expenditure of massive sums of capital, it was an objective that could be pursued without fear of intervention by the competitor arm of the bureaucracy, the Treasury.<sup>1</sup>

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1. The Treasury had made it clear at an early stage that it was strongly opposed to providing cash for an equity stake in commercial oilfields, and indeed it wanted to minimise its share of development costs: see 'State oil deal by Christmas' in The Sunday Times, November 23, 1975.

Secondly, the investment hiatus came to an end in 1976 with several major investments. The Government had provided sufficient assurances on its policies, including majority state participation, to encourage companies and banks to invest capital in field development. For example, the Occidental Group and Thomson Scottish Associates raised about £155m. to finance their share of the Claymore field in February. The chief executive of the International Energy Bank, which organised the financing with the Republican National Bank of Dallas, claimed that international banks were now very confident in the North Sea 'as a lending prospect'.<sup>1</sup>

In conclusion, it can be said that the 'private' face of majority state participation, developed in the negotiations with the various oil companies whose interests would be affected, was one which provided the companies with an assurance that their profitability and access to oilflows would be unchanged in spite of a transfer of legal title to 51% of the oil to ENOC. This assurance was, moreover, articulated in legally binding agreements, which also ensure that ENOC's presence in decision-making is little more than a presence. The scale of these negotiations was simply immense: by February 1976 there had been over 150 meetings on participation in 14 commercial fields, involving the Department of Energy, the ENOC, and representatives of 36 companies;<sup>2</sup> and, to

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1. The Sunday Times, 'Business Diary: Banks ahoy!', February 2, 1976.

2. 905 H.C. (Oral Answer) (February 16, 1976) col.914.



compensate for inadequate staffing, the Government employed legal personnel from the London firms of Freshfields and Herbert Smith.

The objective of showing the course of the participation negotiations in this section has been twofold. Firstly, I wish to emphasise the decisive influence of these private negotiations upon the form of state participation. Secondly, it underlines the ideological importance of the idea of property. The agreements not only had to be acceptable to the oil companies but they also had to legitimate a relationship between oil companies and the state in the eyes of a broader public: hence the Labour Government's determination to secure title to 51% of the produced oil, irrespective of the length of time it took to obtain it. This legal concept lent credence to the view, often expounded in public, that oil was a national resource and was national property.

##### 5. The Establishment of ENOC

The British National Oil Corporation (ENOC) formally came into being on January 1, 1976. However, by the time that the instrument of majority state participation had been fashioned, the definition of participation had changed to such an extent that it was not clear what the instrument was intended to achieve. In addition, the constitution of the corporation contained many peculiarities: the circumstances of its birth had left ENOC with powers best suited to an active, interventionist role, while the

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'option to buy' agreements suggested a very different role for ENOC, as trader in crude oil.

In this section I shall demonstrate not how the state oil company was established but how it was established as a quasi-private concern. The important point here is not that 'private' functions of the ENOC were separated out from public ones in the parliamentary debate on its constitution; but rather that such a separation was only partly successful.

It is impossible to explain the establishment of a state oil company by reference to economic factors alone. It was not necessary to create a large new public corporation in Britain simply to increase the share of revenue accruing to the Government: that could have been achieved by a combination of taxation and royalties. Similarly, a corporation was not required to apply restrictions on the rate of depletion of the reserves under the Petroleum and Submarine Pipe-Lines Act 1975: this was to be undertaken by the Department of Energy. Indeed, the range of regulatory controls to be excluded from ENOC's supervision was so extensive that an editorial in the 'Financial Times' asked: what is left?<sup>1</sup>

The motives for establishing ENOC were in fact political and, as political circumstances changed, so too did the objectives of the state oil corporation. The political pressures which gave birth to the corporation sketched out in the Petroleum and Submarine Pipe-Lines Bill in April 1975 proved temporary. Originally, the

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1. 'Unnecessary oil deal', January 6, 1977.



Labour Party had claimed that, if elected, it would take a majority controlling interest in offshore oilfields.<sup>1</sup> While not bound in any constitutional sense by this manifesto commitment, the highly unstable political climate in 1973-4 had created a crisis of legitimacy in Britain which had, as one of its consequences, the effect of elevating the status of both Labour Manifestoes in 1974. From February onward, there was a tendency for the Government to justify its actions by reference to the appropriate manifesto: a fact of political life much commented on at the time.<sup>2</sup> 'Control' of oil 'multinationals' was an important plank in securing acceptance of the Labour Government's right to govern. However, this political consideration became far less important in 1975-6, leaving the Government far less constrained by election commitments to exert 'greater public control'. Nonetheless, state participation in some form, implying a majority controlling interest, with BNOC as agent, remained essential to the political credibility of the Government.

The establishment of BNOC was accompanied by a process of de-politicisation of its future role. This was done in two ways. Firstly, amendments made to the corporation's constitution during the Bill's passage attempted to distinguish economic from political functions, to fetter the latter and to define them in purely administrative terms. Secondly, the chairman of the corporation,

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1. See the Manifesto of February, op.cit., p.3.

2. For example, John P. Mackintosh, 'The declining respect for the law', in Why is Britain becoming harder to govern? (ed. Anthony King), pp.74-95.

Lord Kearton, expounded a view outside Parliament from 1975 onward which presented BNOC as a quasi-private corporation, engaging in purely economic activities. The Corporation would, he claimed, act according to 'ordinary commercial criteria'.<sup>1</sup> I shall now look at both of these in turn.

The principle of a national oil corporation was opposed in Parliament by the Conservative Party, although as I have already shown at least some senior members of the Labour Government had little enthusiasm for it. Outside Parliament the oil companies and the large banks did not oppose the idea but certainly opposed many of the BNOC's proposed powers. The general context in which the parliamentary debate took place should be noted: not only was there a hiatus of investment in field development, but the press (or at least the influential section of it) carried many reports of speeches and statements made by private interests about the 'error' of state participation and its present and future consequences. One company, Amoco, even placed full-page advertisements in the principal newspapers criticising the Government. Other companies responded less directly, by placing 'informative' advertisements in the press, explaining (and justifying) their role offshore.

The constitution of the corporation proved sufficiently controversial to occupy much of the discussion time allotted to the Petroleum and Submarine Pipe-Lines Bill. The debate focussed

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1. For example, in his first public speech as chairman-designate, reported in The Financial Times, 'State oil corporation will act commercially', October 2, 1975.



on the principle of a ENOC: whether or not there ought to be a state oil company, and on the particular functions of the new corporation. The major sources of contention in the latter category were the following:

- (1) the advisory role of ENOC.

Clause 1 (2)(c) of the Bill required the presence of two civil servants on the Board of the Corporation to assist it in the performance of its obligation 'to tender advice to the Secretary of State with respect to any matter connected with petroleum'.<sup>1</sup> Besides allowing for a considerable degree of communication between the ENOC and the Department of Energy, this provision ensured that ENOC would be subject to a greater degree of state control than most state oil companies, and particularly more than BP. It is a provision unprecedented in legislation establishing public corporations to carry on industrial and commercial activities in the UK, and was heavily criticised by the Opposition.

The presence of civil servants on ENOC's board seemed to threaten the distinction between the 'commercial' or quasi-private functions which it would carry out, and the political, advisory role which it was also to have. ENOC might well be put in situations where it would have access to the (confidential) commercial plans of the companies with which it was competing, giving it an unfair advantage. The Government's response to this criticism was to point to clause 31 of the new model clauses which prohibited the disclosure to any person not in the service or employment of the Crown of returns

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1. Clause 3(3).

made by companies to the Department of Energy in pursuance of licence obligations: according to clause 1(4) of the Bill, the BNOC was not a servant of the Crown, and therefore confidentiality would be preserved. In addition, the civil servants were not to have a vote in the board's discussions,<sup>1</sup> and were not necessary to make a quorum, allowing the other members to meet without them! The Government insisted that the Corporation's status vis-à-vis third parties would be that of Government consultant and these parties' consent would be required for disclosure of confidential information by servants of the Crown to BNOC.

The opposition to this provision was not only considerable (the House of Lords removed the civil servants from the board, only to have them put back on by the House of Commons at a later stage in the Bill's passage), but it is also a comment on the relative failure of dirigisme in the United Kingdom. In France, by contrast, the presence of civil servants on the boards of nationalised industries is common: there are 5 on the board of Electricité de France, 3 on ELF, 6 on ERAP (both oil companies), and 2 on the Compagnie Française des Pétroles. Outside France, all the members of the Danish Natural Gas Organisation are civil servants, and in Italy, 5 out of 14 members of the board of ENI, the state petroleum company, are civil servants.<sup>2</sup>

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1. Schedule 1, para.5.

2. John Smith, the Under-Secretary of State for Energy, made this comparison in the Committee proceedings (June 12, 1975) in cols.361-3.



## (2) BNOC's commercial activities

The commercial activities of a corporation not subject to the laws of the market clearly presented a threat to the private companies operating offshore, and this theme was taken up by the Parliamentary Opposition. The Government replied by giving many assurances that BNOC's commercial activities would not lead it to compete unfairly with private companies: when in partnership with them as a co-licensee it would act like a private company.<sup>1</sup> When acting as an agent of the Government, the Corporation would be in the same position as any private undertaking performing such activities for the Government.

However, the financial position of BNOC seemed to contradict these assurances. Clause 9 of the Bill exempted BNOC from paying the new Petroleum Revenue Tax, which provoked the criticism that unfair competition might result: if BNOC was to act commercially, why did it not pay the special tax like the other licensee companies? It was also an unusual provision for a nationalised industry: the British Gas Council was not granted a similar exemption on its North Sea operations, and the BNOC itself had to pay corporation tax. The outcome of the debate was a Government amendment which compelled the Corporation to calculate its hypothetical liability on PRT and the consequent effect of that liability on its corporation tax liability and to publish this figure in its annual report.<sup>2</sup>

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1. For example, H.C. Deb. Standing Committee D, col.477 (June 17, 1975); 363 H.L. Deb. col.1936 (August 7, 1975); 364 H.L. Deb. col.374 (September 24, 1975); 365 H.L. Deb. col.527 (October 29, 1975); 365 H.L. Deb. col.1761 (November 11, 1975).
  2. 365 H.L. Deb. cols.533-38 (October 29, 1975). Another objection which the Conservatives made to the original proposal was that it might lead to the imposition of penalty taxation against British oil companies operating abroad, particularly since it might unfairly prejudice the North Sea operations of American oil companies: 365 H.L. Deb. cols.387-97 (September 24, 1975).

## (3) BNOC's finances

The method of financing BNOC also gave rise to extended criticism. Under clause 40 of the Bill a National Oil Account (NOA) would be established as the centre of BNOC's financing. All payments would be made into the NOA from royalties and rents to the Government, and the revenues from participation in crude oil trading would also go into this account; and all expenditures incurred by BNOC would be met from it. The Opposition was concerned both with what seemed like a lack of proper accountability and a lack of candour about the scale of borrowing required to fund BNOC's operations.<sup>1</sup> Would the Corporation's activities not lead to a massive increase in state expenditure? In reply, the Government spokesmen claimed that BNOC's expenditure would in fact be subject to 'normal' Treasury control and that its role justified exemption from payment of PRT.<sup>2</sup> Nonetheless, they made several amendments designed to 'make it easier to see what is happening'.<sup>3</sup> The Corporation's financial duties were to be published and specific assurances were given that the Government would take into account the sort of return expected by a private oil company,<sup>4</sup> that before the financial objectives were set Parliament would be informed about them,<sup>5</sup> that

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1. H.C. Deb. Standing Committee D, cols.1627-76 (July 15, 1975).

2. loc.cit.

3. 365 H.L. Deb. col.527 (October 29, 1975).

4. H.C. Deb. Standing Committee D, col.811 (June 26, 1975).

5. loc.cit.,cols.811-12.



exemption from petroleum revenue tax would not be allowed to confer an advantage on BNOC over its partners or competitors when it comes to appraising investments.<sup>1</sup> The Government also agreed in principle to ensure that in its annual report BNOC would give details of its non-commercial activities, but it might exclude matters like the financial details of its subsidised canteen!<sup>2</sup>

In general, the Opposition's argument was that a BNOC was not necessary. There was no need for a state oil company when private oil companies were quite willing to undertake the work of exploration and field development. Why use public finance when private capital was readily available for this work? It must necessarily lead to an increase in state expenditure and perhaps also inhibit further private investment. They also argued that extra regulation, where necessary, could be carried out by an Oil Conservation Authority, which they proposed to establish.<sup>3</sup> While not accepting this argument, the Government response was in general remarkably weak, meeting the Opposition on its own ground. For example, it asserted repeatedly that some tasks might not be sufficiently profitable or might be too risky to be carried out by private companies, thus providing a role for the Corporation. This implied a thoroughly secondary role for BNOC, subordinate to the private companies. By contrast, the

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1. H.C. Deb. Standing Committee D, col.953 (July 1, 1975).

2. 365 H.L. Deb. col.540 (October 29, 1975).

3. 896 H.C. Deb. cols.1301-1346 (July 28, 1975).

principal *raison d'être* of BNOC received little emphasis: the function of holding the interests secured by the agreements on participation negotiated by the Secretary of State in pursuance of the Government's policy of majority state participation in commercial fields. There were only two references to this in the Bill.<sup>1</sup> Perhaps the low profile given this function by Government spokesmen in the parliamentary debate was due to its association with 'politics' and 'sovereign power', the very qualities which might seem incompatible with the claim that BNOC would 'act commercially'.

Despite several hundred amendments to the Petroleum and Submarine Pipe-Lines Bill, many of which concerned the constitution of the BNOC, the Corporation was formally established on January 1, 1976, and the chairman, Lord Kearton, then proceeded to give it a role which corresponded to the grand one implicit in the Act and in the idea of majority state participation. His success in doing this was partly due to his recognition that by this stage the political origins of BNOC had little connection with its final form as a quasi-private corporation, and partly due to his appreciation that a state oil company was an important asset to British capitalism at a time when economic rivalries among the advanced capitalist states were increasing, and fears about the security of oil supplies from OPEC sources showed no signs of disappearing.

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1. In clause<sup>s</sup> 2(1)(e) and 41(1).



Under Kearton's direction it was stressed that the ENOC did not intend to interfere in companies' rates of return from commercial oilfields. Its objectives of limited physical possession and information were met in three ways:

(i) ENOC became a holder of the licence on a joint basis with the other licensees;

(ii) ENOC was granted an option enshrined in the operating agreement to acquire the relevant percentage of petroleum in which it would have some form of beneficial ownership and in return for which it would pay the relevant company or consortium who would otherwise have received the petroleum for the current market price.

(iii) ENOC became entitled to be represented on all committees set up under the operating agreement with a vote to make its presence felt.

However, this was not in itself sufficient. Both Lord Kearton and the Government wished to demonstrate publicly that the new oil corporation was an active one, with as important and extensive a range of activities in the North Sea as any major oil company. Hence during the fifth round of licensing in 1976-7 (the first one since 1972), much publicity was given to ENOC's involvement. It was however a very small round of licensing in which a mere 44 blocks were allocated, compared with 348 in the first round and 282 in the fourth.<sup>1</sup> This was less than half the size of the smallest of the first four rounds, the third (1969), in which 106 blocks were allocated. In addition, objections from the oil

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1. See the Petroleum (Production) Regulations 1976 S.1 1976 No.1129.

companies persuaded the Government to abandon the idea of carried interest for ENOC in this round.<sup>1</sup>

The small size of the fifth round was an indicator of the stage reached by North Sea oil development, by the time ENOC arrived on the scene. It had now become clear that the oilfields discovered under the very large number of licences which had been allocated in the first four rounds were the ones which would allow Britain to reach 'self-sufficiency' by 1980. They were probably the biggest oilfields and certainly the ones which presented the fewest problems of access. Future rounds of licensing would therefore tend to be much smaller.<sup>2</sup>

Lord Kearton himself seems to have been aware that ENOC had arrived in the North Sea rather like Hegel's owl of Minerva: after dusk! Giving evidence to the House of Commons Select Committee on Nationalised Industries in 1978, he admitted that the largest fields had now been found and that the risks and the cost of developing smaller fields made them far less attractive to the oil companies.<sup>3</sup> And more recently, the Corporation claims in its annual report that

The fields will be smaller, more difficult to produce, some in deeper water. There will probably be more projects of smaller average size, but they will call for ever more sophisticated technical skills.<sup>4</sup>

Further support for this view came from a detailed report submitted by the UK Offshore Operators' Association to the Energy

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1. UK Offshore Petroleum Production Licensing: Fifth Round, A Consultative Document, Department of Energy, May 1976, esp. Appendix 1, s.9.
2. The sixth round (1978) resulted in the allocation of a mere 42 blocks. A further round is in progress at the time of writing but the result is not yet known.
3. Seventh Report from the Select Committee on Nationalised Industries, Reports and Accounts of the Energy Industries (1977-8) H.C. 583, pp.45-6.
4. The British National Oil Corporation, Report and Accounts, 1979, p.4.



Commission in 1978.<sup>1</sup> Apparently, the 161 exploration wells drilled by the end of 1974 made 37 discoveries, while the 184 exploration wells drilled in the period 1974-7 resulted in 40 further discoveries. However, of the 8 major fields discovered in the North Sea by 1978 (i.e. those exceeding 500 million barrels of theoretically recoverable oil), only one was found in the latter period. The report concluded that

... the existing commercial fields are thus concentrated in the earlier period of exploration, during which about eleven of the fifteen million barrels of the total theoretically recoverable oil were discovered. This general shift towards smaller discoveries confirms general industry experience elsewhere in the world that the major fields tend to be found earlier in the exploration history.<sup>2</sup>

The overall success in exploration drilling, as measured by the ratio of total exploration wells to those wells which found some oil, has been quite good by average standards, but it reached its peak in 1974, and has deteriorated since. The other important measure of prospects is the size of discoveries, and success in finding larger fields has declined dramatically. The report claims that

While about one well in five has found some oil, only one well in fourteen has discovered fields expected to be commercial under existing fiscal arrangements.<sup>3</sup>

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1. Exploration and Development of the UK Continental Shelf, paper by the UKOOA, October 1978.

2. op.cit., p.4.

3. ibid.

In spite of this, the Corporation had considerable relevance for British capitalism as a whole, as became apparent from early 1979 with the onset of a second 'oil crisis'. The proprietary interests in produced oil which the Government had obtained through the various participation agreements gave it some power to influence its destination. At a time of crisis when the American and European companies who owned the bulk of it might wish to divert it elsewhere, the BNOC could take up its options and keep a portion of it in the UK. This had particular relevance to Britain's membership of the EEC: if supplies of oil from OPEC sources were interrupted, some member states of the EEC, like Britain, might wish to conserve their oil and gas reserves for their own uses, while others, less well endowed with petroleum reserves, might wish to assert a principle of Community solidarity and share the Community's reserves. By obtaining proprietary control through BNOC of 51% of the oil extracted from the UK Continental Shelf, the Government could, if necessary, secure the use of that oil in Britain rather than elsewhere in Western Europe, without imposing regulatory restrictions on exports which would clearly contravene Article 34 of the Treaty of Rome.<sup>1</sup> This had the effect of increasing Britain's bargaining power within the EEC.

Majority state participation, through the BNOC, therefore made no essential difference to the interests and economic activities of the existing licensees. The new legal arrangements

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1. Treaty establishing The European Economic Community, Rome, March 25, 1957. Article 34 forbids such restrictions on intra EEC trade; although it might still be in breach of Article 37 if it followed such a course.



for licensing were both a response to the growing complexity of oil development in the North Sea and an attempt to find a relationship between oil companies and the state which would win popular approval. The latter points to the ideological role of the law in this case: for example, the electorate had to be persuaded that it was majority state participation that was being introduced and hence the figure of 51% was insisted upon. Had the Government merely wished to obtain 'security of supply', this could have been achieved just as effectively with 33% of a licence interest. Besides, in a national emergency a Government would probably make the appropriate new rules whether it was the majority shareholder or not.

Nor was the ideological factor an accidental by-product of the legislative process. Throughout the period 1974-77, it helped to present a picture of radical change in oil policy initiated by the Government, in spite of the fact that its attempts were thwarted at almost every turn both by the vulnerability of British-based international capital, and by the dependence of the state and much of domestic capitalism upon the oil companies for future revenues (to alleviate balance of payments problems, etc.). While sweeping changes in the form of state intervention were indeed introduced in 1974-77, the element of discontinuity in law and policy, and of disagreement between the two major parties was not as great as their speeches and statements tried to suggest. The Conservative Party was in the process of rethinking its policy on North Sea oil, and the Labour Government (as I have shown) was

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unclear before late 1975 about the form of its most radical innovation, majority state participation.<sup>1</sup>

A major difference did arise, however, over the Government's justification for its action. Government spokesmen justified the changes in proprietary interests in two ways: firstly, they claimed the Government was merely altering the regulatory environment in which licensees conducted their operations (a very dubious argument in law), and, secondly, that the Government was obtaining property in most of the produced oil through state participation, as a result of negotiations voluntarily entered into by the licensees. Again and again they claimed that oil was one of those essential natural resources to which the nation-state has prior claim over any private interest or interests. By contrast, criticism of the Government action by both the Opposition and the oil companies emphasised the contractual character of the petroleum licence, and the proprietary character of the rights it conferred. While this emphasis corresponded more closely with reality than the former, the Government insisted upon, and obtained, their ideological victory. At a time when debate about the impact of 'multinational' corporations upon the sovereignty of nation-states was widespread and intense, the British Government appeared to be asserting 'public control' over some of the biggest (and mainly American) 'multinationals'. I shall discuss the significance of this in the next section.

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1. It is a measure of the acceptability of ENOC in its present form to both parties that the Conservative Government, one year after its election, had been unable to think of any major change which it ought<sup>to</sup> make to it: it has confined itself to minor changes which increase the quasi-private character of ENOC, like making it liable to the petroleum revenue tax through the Finance (No.2) Act 1979.



Part II:

Private Property and the State:

some pressing questions

**CHAPTER FIVE:****Property Rights and the State**



It must be kept in mind that new forces of production and new relations of production do not develop out of nothing, nor drop from the sky, nor from the womb of the self-positing Idea; but from within and in antithesis to the existing development of production and the inherited, traditional relations of property.

Karl Marx<sup>1</sup>

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1. K.Marx, Grundrisse, p.278.

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1. The development of capitalism
2. Property rights
3. State intervention



Just as the establishment of a licensing system for petroleum exploration and exploitation was both an attempt to remove obstacles to the commencement of large-scale exploration drilling offshore and also a 'protectionist' instrument for British companies, so the capitalist social system modifies its social and legal arrangements to overcome obstacles to its reproduction and expansion. But how far does this modification go? What are its limits? Since the oil firms succeeded in utilising their licence rights in a manner recalling rights of property, is the change in legal form nothing more than facilitative? Does even a considerable degree of state intervention present no real problems for the profit-oriented large capitalist firms and banks?

In the Introduction I sketched out a theory of capitalist development which I shall now develop with a view to answering these questions, albeit in a rather brief and provisional way. There are two caveats however. Firstly, the object - capitalism and its development - is such a vast one that the following discussion must inevitably take on the character of an outline. Moreover, it is one which, not surprisingly, gives greatest weight to those aspects of capitalism like the state and rights of property which are the principal concern of this study. Secondly, this theory is not an 'appendage' of the foregoing study since it has both informed and guided it; it also provides the basis for the discussion of conceptions of property in the next chapter, a fact which will be apparent from the historical illustrations in the first section.

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# 1. The development of capitalism

The dynamic of capitalist development is provided by the impulse to accumulate. The accumulation of capital establishes a growth in the scale of social production as 'a permanent structural feature of capitalist society'.<sup>1</sup> However, it is also a process which generates contradictions, the temporary solutions to which push the development of capitalism in specific directions.

In a capitalist society, where the money economy is developed, exchange transactions among commodity owners are governed by the impersonal forces of the market. The immediate tie between production and consumption, found in pre-capitalist societies, is broken. Production is no longer geared to local, known needs, and, because there is no definite agency whereby production is adjusted to consumption, there is an inherent anarchy in capitalism. By 'anarchy' I do not mean to imply that it necessarily operates in an arbitrary or chaotic manner, but rather that it runs without central direction. Individual firms or capitalists are free (within limits) to do what they like: to produce what they like and to invest their capital where and how they like, and hence it is an unplanned system. The principal means by which a measure of equilibrium between production and consumption is maintained is the pursuit of profit on capital. A 'crisis' occurs when a sufficient yield on investment is not achieved, and where a significant volume of overproduction occurs, creating a vicious circle in which consumer power is diminished through the

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1. Geoffrey Kay, Development and Underdevelopment, p.77. A good account of the following is contained in Anthony Giddens, Capitalism and Modern Social Theory, pp.46-64.



laying off of labour and a further decline in the rate of profit. The occurrence of a crisis and its resolution eventually recreates equilibrium conditions, but a lower productive capacity, from which a new upswing in production may then commence.

Three sets of tendential properties can be distinguished in capitalism: a tendency for the rate of profit to fall; a tendency toward endemic crises of overproduction; and a tendency toward concentration and centralisation, all of which have the effect of partially undercutting capitalism's own premises. The latter tendency, for example, can serve in part to counter the anarchy of capitalist production. In a monopoly situation, corporations are potentially able to regulate prices and therefore profits in a direct fashion as well as to regulate the needs of consumers, even if only by the exclusion of certain alternative products. Similarly, the centralisation of the market, that is the amalgamation of different firms into much larger units, and manifested in the domination of a limited number of financial or credit agencies, can introduce an important element of regulation of market operations.

The intervention of the state has had a similar role in removing impediments to the process of accumulation in the post-war period in all the capitalist societies. Earlier, the state had played an important role in fostering capitalist development in countries like France and Germany. However, this role has been generalised to all capitalist societies since 1945. The state has

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effectively intervened to tackle certain weaknesses in capitalist economies, and this implies a significant degree of conscious recognition on the part of governmental agencies of the need to rectify or alleviate the 'pathological' tendencies in the system. The 'mechanics' of capitalist production itself do not give rise to such a development.

However, the Keynesian strategies of the advanced capitalist state represented a solution to one series of constraints or impediments to the accumulation process at a particular stage of capitalist development which have turned themselves into impediments constraining the process of accumulation in the subsequent stage. In other words, the 'solutions' have only a temporary efficacy before themselves generating new impediments which constrain the accumulation process. As Erik Olin Wright comments:

It is in this sense that the impediments to accumulation can be considered contradictions in accumulation rather than merely obstacles to accumulation.<sup>1</sup>

They are contradictions because the 'solutions' to a particular impediment become themselves impediments to accumulation, which must in turn be removed for capitalist production to continue. Not that these obstacles are necessarily the same ones each time, but are rather a different series of constraints appearing at different stages of capitalism's development.

In addition, they cannot be passively accepted by the capitalists

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1. Erik Olin Wright, Class, Crisis and the State, p.112.



themselves. As individuals, they must try to overcome these obstacles simply in order to survive in a competitive world, while, as a class, they must attempt to remove them in order to contain class conflict. Accumulation underpins much of the ideological legitimization of the inequalities of capitalist society. The 'ever-expanding cake' allows for a steady increase in the standard of living of the working class and helps legitimate the vastly higher standard of living of the capitalist class. Consequently, a prolonged period of 'no-growth' must seriously undermine such legitimations and lead to an intensification of class conflict.

Every capitalist enterprise (and every capitalist nation) is thus driven to expand its own capital at the expense of other enterprises (and of other nations if necessary). Nonetheless, one major response to the constraints on accumulation is to limit the degree of competition among capitalist firms by a process of concentration and centralisation of capital units, as I have already mentioned. Historically, the scale of production in the successful firms has increased, and more and more direct methods of integration have allowed different firms to collaborate with each other. As I showed in Part I, the principal form of such centralisation in offshore oil development is the joint venture arrangement, which allows several different firms to participate together, thereby spreading the risk. This represents a recognition of the limits of a 'pure' private enterprise system. However,

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despite the introduction of forms of social control by private firms and the state, the capitalist mode of organising production has again and again proved too restricting. For example, the national framework of capitalist operations ceased to be adequate to the expansionist drives of the largest corporations and banks and compelled them to extend their operations abroad. Raw materials enterprises, like the oil companies, were among the very first 'multinational' corporations, quickly extending their interests across the globe into every continent. Indeed, even by the first decade of the twentieth century their ruthless expansion and cut-throat competition was so well documented that their operations provided Lenin with extensive illustrative material for his theory of imperialism.<sup>1</sup>

There was nothing metaphysical about this expansionist drive. The fall in the rate of return on capital invested in traditional areas provided the basis for the imperialist imperative.<sup>2</sup> Capitalism became a world system in order to overcome one specific obstacle to the process of accumulation: the tendency for the organic composition of capital (or the 'fixed element of cost', as economists call it) to rise and to lead to a fall in the rate of profit. The high level of capital intensity reached at the very end of the nineteenth century led to a qualitative change in capitalism.

The logic behind this development can be explained fairly simply.<sup>3</sup>

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1. V.I.Lenin, Imperialism.

2. Although another important incentive was provided by the need to alleviate class conflict. As Cecil Rhodes remarked: 'The Empire, as I have always said, is a bread and butter question. If you want to avoid civil war, you must become imperialists'; cit. in Lenin, op.cit., p.94.

3. This paragraph relies heavily on the account in A.Sohn-Rethel, Intellectual and Manual Labour, pp.144-7.



A growing capital intensity and a rising organic composition of capital leads, at a certain stage, to a change in the costing structure of production amounting to an increasing dominance of the indirect or fixed element of the cost. This element does not vary with output and still remains constant even when production might have to halt temporarily as in a deep recession. These invariable overheads are made up of the interest on borrowed capital, depreciation, insurance, maintenance, leases, rents, and so on. If this part of the cost is high relative to the direct costs (i.e. materials and wages which vary according to the volume of output), the firms concerned will not be able to respond easily to the kind of regulation brought about by the market mechanism. In other words, if demand recedes and prices begin to fall, production ought to be cut back and supplies be diminished: however, the heavy overheads will cause unit costs to rise with a reduced output, with the paradoxical consequence that adaptation of supplies to falling demand forces the cost to rise when prices fall. The consequence is that the rising organic composition of capital makes production increasingly inadaptable to market regulatives. The firms affected by this must react in such a way as to obtain control over the movements of the market, simply as a matter of survival.

It was this reaction which Lenin viewed as the major source of the monopolising tendencies which were clearly visible by the late nineteenth century, after a long depression from 1873-4 to the 1890s, comparable to that of the 1930s. The decline in the

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rate of profit was felt most acutely in the very industries with the highest organic composition of capital, like synthetic chemistry, electricity, and heavy iron and steel manufacture.

These monopoly tendencies sparked out a remarkable debate among social theorists of differing perspectives as to their significance. Many 'new' and familiar ideas about 'organised capitalism' and 'corporatism' had their origins in this period. For example, Rudolf Hilferding argued in his book, 'Finanzkapital', that industrial and banking capital had become closely connected as a result of the banks' provision of the large sums of money-capital required for large scale industrial production. A new combination of industrial and commercial interests (finance capital) pressured the state into a deliberate policy of expansion since 'finance capital needs a state which is strong enough to carry out a policy of expansion and to gather in new colonies'.<sup>1</sup> State protection of industries was directed less at establishing monopoly positions for domestic companies at home than toward establishing monopoly positions abroad and national political power was used to secure markets for capital export, and sources of raw materials. The nation-state had the task of protecting the large investments made by finance capital worldwide in their competition with other national firms. By contrast with Hilferding's emphasis upon the organising tendencies in the 'new capitalism', Lenin

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1. Finanzkapital, p.300; cit. in M.Barratt Brown, The Economics of Imperialism, p.64. Hilferding's principal work has not yet been translated despite the considerable influence it had. The argument is summarised and criticised in Paul Sweezy, The Theory of Capitalist Development, pp.258-69; 294-306.



emphasised its potential for social disintegration: the ordered division of the world's markets, for example, constituted merely a temporary truce in an economic war and ultimately the rivalry among nation-states would break out into war.

In the decades after the 'Great Depression' of the late nineteenth century, capitalism relied on the fulfilment of two conditions for its reproduction and expansion. Firstly, there had to be an expansion of the existing markets by opening up new territories and resuming colonial expansion on a new scale, a path easier for wealthy countries like Britain, France, Holland, and Belgium. Secondly, a substantial increase in the rate of exploitation of the labour employed in the industries at home was required. Industrial 'rationalisation' along the lines of 'scientific management' accompanied the imperialist drive across the world.<sup>1</sup>

While these conditions had proved spectacularly insufficient by the 1930s, the period following the Second World War saw the most successful solution to the problems of accumulation which had ever been achieved in capitalism. A combination of unrepeatable features like cheap and plentiful supplies of Middle East oil and, in some countries, a weak or non-existent degree of unionisation, and also extensive state intervention, led to a 'post-war boom' which lasted until the late 1960s.

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1. At the same time (1895) as Cecil Rhodes made his remarks about imperialism being a 'bread and butter' question, Frederick Winslow Taylor introduced his work to the American Society of Mechanical Engineers with a lecture entitled 'A Piece Rate System, being a step toward a Partial Solution of the Labour Problem'.

During this period the structure of private ownership underwent two major changes. Firstly, basic industries like coal, steel, communications, energy, and transport, were nationalised by the state, thus establishing a large public sector in most of the advanced capitalist societies, and giving rise to the idea that this was a 'mixed economy'. Nonetheless, these industries were no longer proving profitable to private firms, and, once compensation was paid, a state takeover freed the firms concerned to invest their capital elsewhere at a more acceptable rate of return. The operation of the nationalised industries proved the general rule that state-induced competition is non-competitive, being primarily concerned with goods and services that have no place in the market. The appearance of a 'mixed' economy with a public as well as a private sector tended to conceal the fact that there was still only one capitalist economy in which the state had a supportive role.<sup>1</sup> Secondly, there was a remarkable growth in legislative regulation of the rights to use, and to dispose of property. A variety of legal instruments developed to allow state regulation of economic activities and many of these, like licensing, placed a considerable degree of discretionary power in the state bureaucracy. This development provoked some concern among academic lawyers about the control of such discretionary power.<sup>2</sup>

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1. See the discussion in Mattick, op.cit.

2. For example, G.Ganz, 'The Control of Industry by Administrative Process', Public Law (1967), pp.93-106; G.Ganz, 'Allocation of Decision-Making Functions', Parts I and II, Public Law (1972), pp.215-231; and 299-308; H.Street, Justice in the Welfare State, pp.69-96; and Glanville L. Williams, op.cit.



Other regulatory instruments, like those of compulsory purchase, respected the owner's right to benefit, though not necessarily to use and to alienate.

Some writers interpreted these legal modifications to the capitalist framework as evidence that private property was being 'undermined'.<sup>1</sup> As a consequence, the liberal conception of property would have to be 'redefined'.<sup>2</sup> Yet a more plausible interpretation of this phenomenon is that private ownership was in some cases proving to be an obstacle to capital accumulation in the nation-state. At the time when these incursions into private ownership took place, the international rivalry which Lenin had noticed much earlier had given way to a rivalry between two opposing social systems, capitalist and communist, with a limited competition among the advanced capitalist states under the dominance of the USA. It is in response to this international competition that capitalist economies became increasingly organised, although this tendency has never gone so far as to abolish competition within any particular nation-state, merely limiting it somewhat. Failure to socialise a particular industry in decline, like the coal industry, might have led to a cessation of production in that industry, and a consequent decline in the competitive position of the national capitalism vis-à-vis other national capitalisms. In the case of coal production, failure to produce at a profit under private ownership and direction rendered

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1. Stein and Shand, op.cit.

2. W.Friedmann, op.cit.

the future of the coal industry in Britain problematic. The assumption of ownership and management by the state secured a basic fuel for the national capital units (and also secured the votes of the large number of miners involved). Similarly, subsidies to private producers, expenditure on military and space programmes, as well as on welfare, education, and social security, were essential components in maintaining social and political stability, and in the reorganisation and expansion of capitalist production after the Second World War.

State regulation has had a similar role in the North Sea. As I have shown, the adoption of a system of discretionary licensing had advantages for British capitalism in an environment which was, from the outset, certain to be dominated by the superior expertise and greater capital resources of American firms. Perhaps it is no accident that the only serious advocate of an auction system of licence allocation for the UK Continental Shelf is an American.<sup>1</sup> After 1974, non-fiscal state intervention had as one of its goals the administrative one of reorganising the ad hoc arrangements which had been set up during the preceding decade. The BNOG, for example, had as one of its less publicised goals that of centralising the various forms of state participation which had been introduced during that period. This, and other aspects of state regulation between 1974 and 1977 might suggest that the quasi-

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1. K.W.Dam, Oil Resources. This would certainly have resulted in a greater proportion of American companies obtaining licences than under the discretionary system.



proprietary function of licence rights was being 'undermined'. Yet I have shown in some detail that this was very far from being the case.

This growing international rivalry does not of course have the same consequences for all property-owners. The close relationship between the largest capital units and the state has been remarked on frequently since the beginning of the twentieth century. A close involvement with the internal structure of the state allows the holders of large scale property to ensure that obstacles to further capital accumulation which can be surmounted by legislation are tackled by legislation which they themselves have had a hand in drawing up. This can be achieved as the oil companies did in 1974-5, through extensive consultations with the relevant Government Department. It was just such a relationship between large firms and the state apparatus which led Pashukanis, the Soviet jurist, to contrast the attitude of capitalists toward property rights in the nineteenth century, where the owners' freedom to use, to alienate and to benefit was treated with a special reverence, with the 'ad hoc' approach characteristic of monopoly capitalism.<sup>1</sup>

This modified attitude has its roots not only in a perception on the part of capitalists of the need to place the removal of potential impediments to capital accumulation above ideological considerations, but also in a series of changes in the capitalist class itself. John Scott has recently written extensively on this

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1. E.B. Pashukanis, Law and Marxism, pp.129-30.

phenomenon of 'depersonalisation' of property-ownership which lies behind these changes.<sup>1</sup> Capitalist development led to the replacement of a dominant class composed largely of individual entrepreneurs, family firms, and rentiers, by one in which such elements play only a very minor role. The major role is played by large industrial firms, banks and institutional investors. It is just this 'faceless' dominant class which, as Harris notes, no longer needs

... to commit itself to the defence of private property as first principle, much less the defence of the mass of small private property owners.<sup>2</sup>

The ability of these owners of productive property to develop and utilise close links with the state apparatus, rather than simply the governing party, means that they have less need for a general theory of property rights and the state, which might inter alia set out limits to the 'public sphere' in a systematic way.

Furthermore, it was just this very group of large-scale capital units which benefited most from the post-war boom in capital accumulation. Throughout this period, and at the same time as the state's role was being deliberately expanded in all the advanced capitalist countries, there was a continuous movement toward interpenetration and interdependence of trade, investment and

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1. J. Scott, op.cit.; see also Lucio Colletti, From Rousseau to Lenin, pp.45-108.

2. Nigel Harris, Competition and the Corporate Society, p.249.



finance. Restrictions on trade and capital movements constructed during the 1930s and during the Second World War were systematically dismantled. Linked to this expansion of trade, export of capital, and establishment of production worldwide, was the development of a stable international monetary system, dominated by the American dollar. The economist, Andrew Shonfield, has claimed that

The great postwar movement of liberalisation in international trade in the West can be regarded in part as a by-product of this curious and necessarily impermanent monetary relationship.<sup>1</sup>

It is this context of the internationalisation of capital and the consequent intensification of competition among national capitalisms that state intervention in the national economy has to be understood. Those who concluded with Shonfield in the 1960s that economic planning was the most characteristic expression of the new capitalism based their conclusion on stabilising tendencies occurring within the framework of the nation-state, underestimating the extent to which the internationalisation process was, in the longer term, a destabilising one for the system as a whole.

The tendency to generalise about change in the social structure from the particular and limited features of this 'new capitalism' was common at that time. The post-war boom and the unprecedented prosperity it brought to many, although not all people in the advanced capitalist societies, provided the stimulus to a great many theories of 'post-industrial' society. While placing a different emphasis upon

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1. That is, the dollar's role as international reserve currency: Modern Capitalism, op.cit., p.33.

particular changes, they all concluded that 'industrial society' (i.e. capitalism) was on the verge of a transition to a new kind of society which had overcome the conditions of scarcity and the tendency toward slump. These theories were rooted firmly in the 'industrial society' tradition in the social sciences, and now seem, as Anthony Giddens observes, 'almost archaic, following a period of heightened political and economic conflict'.<sup>1</sup>

The changes which seemed most likely to lead to a movement beyond capitalism were bound up with the new interventionist role of the state. The impact of the various forms of state intervention upon key institutions of capitalism like private property and the market was so great that a reappraisal of the dominant concept of property as private property seemed appropriate.

## 2. Property Rights

The process which I have described in the foregoing section in terms of 'obstacles' and 'impediments' to capital accumulation is, obviously, based on Marx's conception of capitalist development as a dialectical relationship between forces and relations of production. At a certain stage in the development of material forces of production in society, these come into conflict with the framework which organises them. When this occurs, the relations of production cease to function so as to fully utilise the productive forces available, and instead they fetter the further development of those

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1. 'The Prospects for Social Theory Today', in Central Problems of Social Theory, p.235.



forces.<sup>1</sup> Marx envisaged the possibility of an integration of various forms of social control into the capitalist economic framework which might defuse the resulting tensions somewhat, but was convinced that they would not have more than a temporary efficacy.

The role played by property rights in this process is complicated by several factors. Firstly, not all property rights have the same social significance. For example, property rights in objects for personal use have little relevance to the foregoing sketch of capitalist development. Many individuals in capitalist societies have personal possessions but they are 'propertyless' in the sense that they do not own a share in the means of social production: their principal marketable 'property' is their power to work. Indeed, the vast bulk of productive property in these societies has remained concentrated in the hands of one small group of individuals, making them a 'class' by virtue of their ownership of the means of production. This is not contradicted by the fact that almost everyone in a capitalist society is nonetheless a subject of legal rights and is therefore capable of becoming an owner of means of production: this attribute is a formal one which certainly does not make them owners of productive property in fact.<sup>2</sup>

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1. See the 1859 'Preface' to A Contribution to the Critique of Political Economy, pp.19-23. By 'forces of production' he has in mind the various means of production like railways, refineries, oilrigs and also the power to work. By 'relations of production' he simply means those relations within which production is carried on, like the work relations in a factory.
  2. Of course, a large number of individuals have a share in productive property indirectly through trade union membership or holding insurance policies. The fact that such institutions have shares in productive property does not, however, give strategic control of these funds to the particular individuals whose 'wealth' is managed by an elite.

While ownership of productive property has a vastly greater socio-economic significance than ownership of objects for personal use, it must be emphasised that this is more than a question of title or of 'holding' capital resources. Capitalists, whether firms or entrepreneurs, are compelled by competition to utilise the objects of their property in order to make profits. For the most part their property in means of production becomes a means by which capital can be accumulated in the form of profit. Hence there is an important connection between modern property and the idea of convertibility. The right to alienate the objects of property as commodities on the market becomes vital in capitalism since all production is geared to the realisation of capital invested and also surplus value.

It was just this feature which attracted the attention of E.B.Pashukanis in his analysis of modern property.<sup>1</sup> In his view, the freedom to transform capital from one form to another distinguished the modern property right from its feudal predecessor which tended to have restrictions imposed upon alienability. It is in these market transactions that the notion of property as a right in the most absolute sense acquires its social significance. In a capitalist society, the legal right of property had its real significance as freedom of disposition in the market and not merely as a means of securing the possession of things vis-à-vis other possessors. The real material basis of modern property rights is the

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1. E.B.Pashukanis, 'The General Theory of Law and Marxism', in Pashukanis, op.cit.



development of a universal market which increases the number of individual owners, competing against each other. Since these individual private interests exist in opposition to, and in competition with, each other, the individual owner must be secure in his right against all other property owners, but it is always a control with a view to alienation that matters to him, and the time, place and manner of the exchange are his own 'business'.

A second complicating factor results from the apparent 'decline' of property rights in the twentieth century. A considerable body of literature now exists on the impact of the modern large corporation upon rights in productive property, and several writers have interpreted it as requiring a firm separation of conceptions of property in legal and economic senses, and a designation of the former as superficial. For example, Nicos Poulantzas notes that 'it is possible for the forms of legal ownership not to coincide with real economic ownership',<sup>1</sup> and then uses 'economic ownership' to mean control of the means of production, or the power to assign the means of production to given uses and so dispose of the products. The trouble with this, and all attempts, to distinguish legal from 'economic' property is that the latter is usually conceptualised in juridic terms like ownership, use and possession.<sup>2</sup>

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1. Classes in Contemporary Capitalism, p.19.

2. For example, Karl Renner, Institutions, p.284. More successful are the attempts to define 'economic ownership' as the power to appropriate the product and to control the work process (Bettelheim, op.cit., pp.134-5; Poulantzas, op.cit., p.18). See also G.A.Cohen, Karl Marx's Theory of History, for a novel treatment of this.

Much of the justification for making such a distinction derives from the perception of a real separation between legal ownership and economic control accompanying the rise of the joint-stock corporation. The thesis that legal ownership has been dispersed among various shareholders and economic or strategic control delivered over to a class of professional managers has been a common one in neo-liberal thought since the 1930s.<sup>1</sup> It sees a divorce between the actual property rights held by a large number of stockholders and rentiers, of whom few owned enough to claim a voice in a firm's direction, and the control exercised by a 'technostructure' motivated less by maximisation of profit than by other goals like status.<sup>2</sup> Similarly, MacPherson argues,

Individual investors of all sorts become rentiers and become aware that this is what they are. Their property consists less and less of their ownership of some part of the corporation's physical plant and stock of materials and products than of their right to a revenue from the ability of the corporation to manoeuvre profitability.<sup>3</sup>

However, there is a growing body of empirical research which shows that propertied interests still play a major role in deciding the destinies of major corporations, even if stock ownership is to some extent diffused. For example, a study by Maurice Zeitlin argues

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1. The ~~original~~ version of this argument was advanced by A.A.Berle and G.Means in The Modern Corporation and Private Property. It was developed by inter alia Ralf Dahrendorf, in Class and Class Conflict in an Industrial Society.
  2. See J.K. Galbraith, The New Industrial State.
  3. C.B.MacPherson, Democratic Theory, p.154.



inter alia that financial institutions have an important role as owners of company interests.<sup>1</sup> Share ownership, through the credit and banking system, still has a central importance in the exercise of strategic control. Empirical research also supports the view that managers of large corporations tend to become large property owners in their own right during their progress toward tenure of managerial positions.<sup>2</sup> However, Zeitlin's approach to this 'separation' breaks away from the individualist focus of liberalism and interprets the development in terms of a managerial reorganisation of the propertied class. He argues:

Although the largest banks and corporations might conceivably develop a relative autonomy from particular proprietary interests, they would be limited by the general proprietary interests of the principal owners of capital. To the extent that the largest banks and corporations constitute a new form of class property ... the "inner group" ... of interlocking officers and directors, and particularly the finance capitalists, become the leading organizers of this class-wide property.<sup>3</sup>

The relationship between legal ownership and strategic economic control in the large concentrations of property is therefore a complex one, and empirical research strongly suggests that the 'distance' between legal and economic structure in this case (that is, productive property) has been much exaggerated. Further, a real basis does not seem to exist for arguments to the effect that

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1. Maurice Zeitlin, 'Corporate Ownership and Control', in the American Journal of Sociology, vol.79 (1974) 5; see also A.Francis, op.cit. who bases his argument on results from the Oxford Growth of Firms project.
2. See Blackburn, op.cit., pp.166-8.
3. Zeitlin, cit. in Scott, p.120. Italics in the original text.

property rights are of declining social and economic relevance. It is certainly true that individual capitalists have less legal discretion today over their holdings than they once did. They have fewer rights over what they own, for example, as a result of legislative regulations over use. However, it does not follow that capitalists as a class have less control over the means of production. A reduction in control by individual capitalists may result from increased control by capitalists as a class through the state.

A final but no less important complicating factor in ascertaining the implications of capitalist development for property rights is that the socio-economic relations which constitute a society rarely correspond exactly to their legal representations. In various remarks which he made on the subject, Marx thought that relations of production 'develop unevenly as legal relations',<sup>1</sup> ~~and that~~ a considerable degree of freedom and equality in law was compatible with, and necessary to, economic exploitation. This irony was possible because legal relationships were predicated on one particular part of the economic structure, the market. Hence generalisations about individual rights based on characteristics of the legal structure were not only bound to contain an element of distortion, but were also likely to prove advantageous to those wishing to conceal or minimise real elements of social inequality.

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1. 'Introduction' to Grundrisse, p.109.



While I am entirely in agreement with the view which sees law and property rights as 'superstructural' and therefore in some more or less complex manner 'deriving' from economic structure, it does seem to me that too much ought not to be made of this insight. Property rights, even when modified to allow some social control over use and so on, still provide the sort of legal assurance required by economic interests in capitalist societies. One may of course conceive of situations in which existing rights of property seem to have scarcely any basis in capitalist economic relations and which even present problems for them, but these will be exceptional situations and will not be found in the more profitable branches of production.

However, changes in economic structure may compel a reassessment of the suitability of specifically property rights for a particular type of economic activity. In particular, the extension of capitalism at a stage in its development when property rights in general are subject to a range of regulatory controls over use, disposition and so on, may be carried out under legal arrangements which allow private interests rights but not property rights.

As I noted above, ownership in general has various incidents not all of which have equal significance for a capitalist. For example, A.M.Honoré claims there are as many as 11 distinct incidents necessary to ownership in the 'full' or 'liberal' sense.<sup>1</sup>

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1. A.M.Honoré, op.cit.

Similarly, some writers have preferred to view property not as a right but as a 'bundle of rights'. Lawrence Becker, for example, argues that

... property rights are typically aggregates of different sorts of rights and rights-correlatives.<sup>1</sup>

The importance of these distinctions is twofold: they allow us to conceive a possible situation in which certain key property rights or incidents of ownership might come to be associated with a non-proprietary legal arrangement over objects or in relation to specific economic activities in which some social control through state regulation is considered essential; and secondly, they help explain why a multitude of statutory restraints can be imposed on certain rights without affecting the essential ones: in Marx's language, the right to appropriate surplus value through the medium of specific legal rights is left untouched.

In the light of the foregoing remarks about property rights in capitalism, I shall now reconsider the licensing relationship examined in detail in Part I.

The petroleum licence is the legal link between the Crown's possession of rights to offshore petroleum resources and private exploration and exploitation of those resources. It is the vehicle by which some of the Crown's rights are transferred to private companies. This is effected principally through model clause 2 which is standard form in all licences: it grants to the licensee

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1. Property Rights, p.21. Cf. W.Friedmann, Law in a Changing Society, and O.Kahn-Freund, in 'Introduction' to K.Renner, *op.cit.*



'exclusive licence and liberty ... to search and bore for, and get, petroleum'.<sup>1</sup> The licensee therefore receives an exclusive right, but a right to what? If one considers it as a right to the oil in place, the answer is not entirely clear. However, it is clear that the licensee will not view his exclusive right in this way. Ownership of the oil in the ground is of little importance to the licensee unless the oil is capable of being extracted and marketed, and unless the owner or licensee has the right to do so. Even then, the licensee will be content to acquire those rights necessary to give effective control over the oil once it is extracted: that is, at the well-head. Whether or not the licensee 'owns' the oil in place is not a question which vexes the companies, nor their lenders, the banks. This was made clear in the discussions on lenders' security when the first generation of oilfields became ready for development in 1975-6.<sup>2</sup>

In relation to other capital units which may wish to operate in the North Sea, the holder of a licence has a better right in his block or blocks than anyone else. He is granted a monopoly right which will be protected by the state which will act to prevent non-licensed companies from drilling. The licence therefore gives the recipient a right which is 'better' than anyone else's right. Whether or not he is an owner of oil resources in place is much less

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1. Petroleum (Production) Regulations 1976, Schedule 5.
2. For example, the paper by G.D.M. Willoughby, op.cit.

important both economically and legally than whether or not his right is good enough to allow him to do x: in this case, x is the extraction and marketing of any oil found in order to make an 'acceptable' profit, the goal of the initial capital investment. The oil companies' assessment of the value of a licence will focus not only on the characteristic of exclusivity attaching to the right transferred, but also on the ability of a licensee to take possession of produced oil and convert it into some other commodity at a profit for themselves. In this sense, oil companies are no different from General Motors, whose business, as Alfred Sloan remarked, is to make money. Once the oil is produced, it can be transported as a commodity to a market and sold, or, alternatively, used as a raw material in the refineries owned by various major oil companies. This right to appropriate which the parties to a licence consortium have, and the freedom of disposition (not in my view significantly affected by BNOC's rights) give a licensee the same kind of economic control as a property owner.

By emphasising the connection between modern property and exchange, Pashukanis' conception of property right (unlike MacPherson's which emphasises the feature of exclusivity<sup>1</sup>) helps to explain why oil companies are so concerned to obtain (and to retain) rights to the produced oil, and are almost indifferent to the question of ownership of oil resources in place.

This does not of course mean that ownership of oil resources

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1. See the next chapter, section 1.



in situ is completely irrelevant, nor that the resources in that condition are without value. Middle Eastern governments who insist on extracting their oil at slower rates than oil companies would prefer, do so in the full knowledge that the remaining recoverable reserves of oil will gain in value as prices rise. In 1979/80 alone, oil and gas reserves in situ in the UK trebled in value as a result of increases in the world oil price.<sup>1</sup> Nonetheless, ownership of oil resources in situ has a completely different economic significance from ownership of the means to explore for and exploit them. From a state's point of view the criteria it adopts to assess its proprietary or sovereign rights have nothing to do with business-directly. The British case illustrates this point.

Through the Continental Shelf Act 1964 the Crown possesses certain rights to which it can lay claim in international law: 'sovereign rights' to explore and exploit.<sup>2</sup> The Act gave the Crown a monopoly of effective control over the UK Continental Shelf. It had acquired a right which it could enforce against other states. That right had an exclusive character being, firstly, a right to prevent others getting petroleum resources, and secondly, a right to extract. The petroleum resources could not therefore be res nullius. This did not represent 'sovereignty' but it did give the Crown the

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1. The Financial Times, 'Oil and gas reserves treble in value', July 21, 1980.

2. The 1958 Convention on the Continental Shelf stated the then customary international law. The latter has changed since that time and therefore the Convention no longer has the last word on the meaning of 'sovereign rights'.

'best' right vis-à-vis other States, which was sufficient for the purposes to which it would be put. Those purposes were not, however, to allow the British state to act like an Exxon or a Shell and develop whatever petroleum resources it might have. The assumption of sovereign rights was merely a prerequisite for the establishment of a licensing regime which had, as one of its goals, the objective of attracting sufficient interest from the oil companies to invest the sums of capital, expertise, and so on, necessary for exploration to commence. Sovereign rights in the oil in place have then quite different economic consequences than the quasi-proprietary rights in produced oil which the licensees are concerned to obtain, and in this case do obtain.

### 3. State intervention

The most visible expression of a 'decline' in the role of property rights in modern capitalism is the interventionist state, especially in respect of its intervention in specifically economic activities. Yet this phenomenon is characterised by two general features which show how paradoxical such a view of the state's role is.

To begin with, state intervention has a remarkably superficial effect on the workings of advanced capitalist economies. As I argued in section 1, state intervention has a reactive character. It is one means by which obstacles to capital accumulation

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can be overcome. Such obstacles have their roots in the antagonistic character of the capitalist mode of production, in which productive forces repeatedly expand faster than the rate at which the production relations can change in order to utilise them. The state's involvement in North Sea operations provides several illustrations of this.

As I explained in chapter two, the initial involvement of the state in regulating North Sea exploration was partly because the technology, equipment, labour and so on, were available but the legal framework for organising those forces of production was inadequate. Companies could have begun exploration drilling, as they had begun making seismic surveys before 1964, but they had no means of restraining competitors from taking advantage of any success they might have. The division of the continental shelf into blocks and the introduction of a licensing system resolved this problem. Similarly, the improvements in rig technology in the late 1960s created the possibility of exploration in the northern sector of the North Sea, and the Government reacted by issuing a large number of licences in two rounds, the third and fourth, between 1969 and 1972. In so far as the individual capital units, in a condition of competition, were not able to provide the basic or general conditions for the utilisation of new productive forces, these conditions were provided by the state.

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In establishing a legal framework suitable for oil development, the state is acting in a manner characteristic of states in capitalist societies. Such states have their origin in the phenomenon of generalised commodity-exchange among property owners, each with his own private isolated interest, each opposed to the other and the united only in the relationship of buyer to seller. As Pashukanis noted,<sup>1</sup> neither of the persons effecting an exchange can emerge as the dominant regulator of that relationship and a third party is required to embody the mutual guarantee which commodity owners give to each other as owners. This third party, the public authority or state, personifies the rule of the intercourse of commodity-owners, and is the guarantor of market-exchange. It is therefore the existence of freedom of competition, private property and equal rights in the market which makes a specific form of public constraint necessary. This does not, however, exclude a monopoly of force, always a feature of states, capitalist or otherwise.

This view of the state serves to underline its irrevocably capitalist character.<sup>2</sup> It also allows for the possibility of a 'relative

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1. See Law and Marxism, pp.134-150, for an account of this; but also see the section on 'public law' in T.S.Midgley, The Language of Equality, Edinburgh University Ph.D thesis (1978).
2. This point is discussed in much of the current literature on the state: for example E.P. Thompson, What Does the Ruling Class Do When It Rules?; John Holloway and Sol Picciotto (eds.), State and Capital; and Colin Crouch (ed.), State and Economy in Contemporary Capitalism.



autonomy' of the state from particular capitalist interests. The state is not a neutral instrument in the hands of a 'power elite'. In the overall interests of the system, the state cannot align itself with some interests as distinct from others - at least not for any length of time. It must pursue the general interest of a national capitalism, if necessary against the interests of individual capital units. This does not lead to the performance of purely peripheral functions: on the contrary, the two notions of 'accumulation' and 'legitimation' group together a series of functions which the state performs and which are of crucial importance to modern capitalism. Under the first heading is included state expenditures on arms, transportation, communications, and similar activities, which have the effect of increasing productivity and the utilisation of industrial capacity. If production is not profitable or else its extent is too broad to be performed by capital units with their special interests, the state can 'intervene' and do the work, since it is not obliged to follow the dictates of the profit-motive. It provides the general conditions of production which private interests could not, of their own accord, provide, and above all provides 'a unified and universalistic legal framework for free enterprise'.<sup>1</sup> Under the second heading, the state carries out activities which co-opt potential sources of popular discontent by attempting to transform political demands into economic demands. The securing of 'majority state participation'

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 1. Therborn, op.cit., p.103.

in existing commercial oilfields by the British Government is one example of this legitimization function: indeed, more broadly, the very activity of legislating has, or is intended to have, this effect. For example, the Labour Government responded to the outbreak of class conflict in Britain in the early 1970s by initiating the biggest legislative programme since the 1945-51 Labour Government: the legislative output of the 1974-5 Parliamentary session was in fact quantitatively greater than the busiest session in that earlier period.<sup>1</sup>

The state's intervention is then a reaction to problems in the economic structure, which is itself the presupposition of the state's existence as a capitalist state. Moreover, that reaction is designed to solve those problems in such a way as to permit the reproduction and expansion of private production both by 'economic' means and by means of securing consent. On this view of the state, it is quite wrong to conclude from the fact of considerable legislative restrictions on private property that they are hostile to private ownership in general.

Another paradoxical feature of state intervention is the extent to which it is accompanied by private intervention in the state. That is, private interests, especially the larger and better organised ones, become more and more involved in the

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1. Keith Middlemas makes too much of this in his book, Politics in Industrial Society. He argues that the British 'establishment' deliberately stimulated a tripartite relationship between big business, trade unions and government during the years 1916-26, which successfully avoided political crises and integrated the unionised working class until the mid-1960s. However, the corporate bias in government is not peculiar to Britain and the systemic forces contributing to it are more influential than the policy directions of the dominant class.



state's extending range of activities. To cope with this, the inner structure of the state itself undergoes changes. This feature is central to the questions of why state intervention assumes one particular form and not another, and which interests secure the greatest benefit from a particular state's intervention: are they industrial or financial, in the main? Are they international or national in their base of operations? If state intervention works principally to the advantage of specifically private interests, does this relegate the actions of social democratic governments to the same role as governments overtly concerned to promote the private interest? These are questions which I do not attempt to answer here, although some light may be shed on them by the empirical study in Part I. My goal here is simply to note that a view which sees the state's intervention as an exercise of 'control' over particular private interests can only be held with considerable difficulty once one recognises that the highly concentrated economic structure of contemporary capitalist societies gives them (at least) a considerable degree of influence over the form of state intervention. As I showed in chapters three and four, this influence can be very considerable indeed, and can be welcomed by a government which publicly espouses a rhetoric of 'control', 'regulation', and the language of sovereignty.

Together these two paradoxical features of state intervention suggest the need for a cautious appraisal of the state's role, and particularly the 'liberal' use of the term 'corporatism'.

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If J.T.Winkler had considered the modifications to the Industry Act 1975 more seriously he might have hesitated to cite it as an example of a trend toward the so-called corporatist state.<sup>1</sup> The importance of this latter point is obvious. If there is a tradition of direct involvement of particular firms in the activities of the state (that is, 'consultations', 'talks', or 'discussions' with a particular Department), then those firms are likely to acquire a degree of assurance of the security of their interests which goes beyond the specifically juridical security visible in the character of the rights which they possess. That this was certainly the case with respect to the activities of many international oil companies, ensured that the rights transferred by the petroleum production licence by British Governments had an aspect of permanence about them which was not, in my view, removed by the events of 1974-77.

Certain social and economic features of capitalism in Britain also contributed to shaping the form of state intervention in this case, showing that, in addition to the broad constraints on capitalist states sketched out above, there are other more specific constraints deriving in part from historical development. Among

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1. 'Law, State and Economy: the Industry Act 1975 in Context', in The British Journal of Law and Society (1975), Vol.2, pp.103-128. A more critical view of the Act, and its implications for the corporatist thesis is provided by Tom Hadden in 'The Industry Act 1975', 39 Modern Law Review (1976), pp.318-21.



the various advanced capitalist societies, Britain occupies a unique position. The first country in the world to industrialise, it also became the first real world power, both economically and politically, extending the capitalist mode of production across large parts of the world. While the status of world power was soon acquired by other countries like the USA and the USSR and Britain's political influence declined, the economic structure of British capitalism continued to reflect the key role in the world economy of many of its economic institutions, principally those in the City of London. However, the largest industrial units like BP and ICI also have important and extensive overseas interests. While both the City and the British-based multinationals have found their international operations extremely profitable, both the domestic economy and the state itself are (relatively) weak, a feature explicable

... not by the simple decline of British capitalism as such, but by the very strength of the cosmopolitan activities of British capital, which has helped to undermine further its strictly domestic economy.

There is then a conflict between the nationally and the internationally operating sections of British capitalism, and the very strength of the former has reinforced the long-term decline of

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1. B.Rowthorn, in M.Radice (ed.), International Firms and Modern Imperialism, p.174. See also Frank Longstreth, 'The City, Industry and the State', in Colin Crouch (ed.), *op.cit.*, pp.157-190.

British capitalism as a whole. Such a conflict was visible in the debate over licensing terms and the policy of rapid exploration. Throughout the 1960s and early 1970s the latter policy worked to the advantage of the large British and American oil companies, even though Governments realised that, as a consequence,

... less time was left for their own indigenous industry to make itself ready to seize opportunities.<sup>1</sup>

Similarly, the overseas interests of BP and indeed all British-based companies operating abroad were an important influence upon the domestic petroleum policy and the choice of licensing terms throughout the 1960s, and also upon the revision of terms in 1974-5: throughout the entire period covered in the empirical study, from 1960 to 1977.

The thrust of this latter observation is this. The close relationship between the largest capital units and the modern state can provide juridical arrangements between private parties and the state (like government contracts and petroleum licences) with a degree of extra-juridical security which might, in the period of classical capitalism, have been contained in the juridical form itself: for example, certain rights might have been designated property-rights. However, an additional element of extra-juridical security is provided for the private interest(s) if it is one which is located among the bloc of private interests traditionally

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1. Sir Robert Marshall, Secretary of the Department of Trade and Industry, in the PAC Report, op.cit., p.141.



favoured by a particular state: in Britain's case, this is 'international capital'. The company concerned may be American and not British-based, but because of the general dominance of 'international capital' over the state in Britain, it shares the same element of extra-juridic security in its interest.

As a consequence of this view I have not dwelled upon the 'corporatist' implications of the panoply of Ministerial controls built into the revised Model Clauses in 1975. Just as we saw earlier that Winkler's failure to give proper weight to the legislative process led him to exaggerate the significance of the final legislation, in this case we must avoid the beguiling character of legal 'appearances'. The regulatory powers contained in the Act were the outcome of intensive and lengthy negotiations between the Government and the parties concerned, as well as a parliamentary debate: while not eliminating the possibility of future conflict over the exercise of these powers this procedure did ensure that it would be minimal, by allowing for considerable modifications in the original proposals.<sup>1</sup> Nonetheless, on the evidence presented in the thesis, it is unlikely that the exercise of these powers would be inimical to the interests of international capital.

While it has not been my intention in this section to provide a general theory of the state, I have attempted in making these remarks to situate legislative restrictions on the exercise of property rights in a broader context, and also to suggest that the close relationship between large capital units and the state ensures

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1. For example, the original depletion power was radically modified (see discussion on pp.168-9 and esp. p.175); other major changes are mentioned on pp.181-2 (esp. p.181, footnote 5).

that the difference between property rights and (some) other rights need not be a matter of great practical import. The point is not that this or that legal alternative would have led to greater 'control' but rather that whatever course of legal action had been adopted, it would still have been subject to the kind of structural constraints which I have set out in this thesis. The basis for a thesis about 'new property' lies here.



**CHAPTER SIX:****The Transcendence of Private Property?**

Contents:

1. New Property - in theory
2. New Property - in practice



# 1. New Property - in theory

The massive extension of the state's role in advanced capitalism has made an increasing number of persons dependent on the state for some sort of guaranteed income. The New Property theorists have taken this particular phenomenon as a basis for an attempt to replace the liberal conception of property with another, more 'general' one.

Their ideas about property are of interest because they constitute one way in which writers with a commitment to liberalism (and I include MacPherson in this category) have attempted to revise classical liberal ideas to 'fit' the circumstances of advanced capitalism. The monopolistic trend of capitalist development in which the large corporation supplanted the family firm of the entrepreneur as the basic economic unit rendered the individualist premiss of the older writings on property less and less satisfactory. However, the problems posed by the interventionist role of the state went to the heart of liberal thinking, since liberalism, as Lukes notes,

May be said largely to have been an argument about where the boundaries of this private sphere lie, according to what principles they are to be drawn, whence interference derives and how it is to be checked. It presupposes a picture of man to whom privacy is essential, even sacred, with a life of his own to live.

This concern with delimiting the private sphere is underlined by

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1. Individualism, p.62. In arguing that capitalism is now a 'post-liberal' society, Roberto Unger also places considerable emphasis upon the changed role of the state: see Knowledge and Politics, and Law in Modern Society.

Gianfranco Poggi who points out that many of the early liberal theories invented devices to secure the private sphere from any incursions by the state.<sup>1</sup> For example, those ideas based on the notion of a natural law: the existence of rights of man, including property rights, prior to and above those of the citizen, or interpretations of constitution-framing reminiscent of the social contract theory.

Ironically, the qualitative change in the state's role in the period after 1945 did not produce the feverish re-assessment of private property that one might have expected from liberals. Without much discussion, the idea became accepted that property rights could be, and in some cases ought to be, restricted in the common interest. Such restrictions occurred if, and to the extent that, legal controls were established which diminished the scope of an owner's powers and freedoms (e.g. of use, disposal, alienation) over the thing he owned. This idea has become so common that even a conservative liberal like Lawrence Becker thinks it necessary to include three kinds of limitation in any specific justification of a general theory of property-rights.<sup>2</sup> Firstly, he claims that there can be no full, liberal ownership in land. Secondly, ownership of vital depletable resources like fresh water, fossil fuels and mineral deposits

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1. The Development of the Modern State, pp.104-7.

2. The following extracts are taken from Becker, op.cit., pp.116-8.



... may have to be restricted to the rights of income, transfer and limited transmissibility, with management, use and actual possession effectively under public control.

He emphasises that this has nothing to do with 'social justice' but rather it follows from this start<sup>ling</sup> admission:

If the necessary conservation measures cannot be guaranteed (with any significant probability) under a system of full liberal ownership by individuals, then something along the(se) outlines ... seems the only rational course.

Finally, he accepts the need to introduce measures to limit accumulations of wealth (for example, by a wealth tax) to prevent such accumulations from undermining 'the democratic ideal' in government.

These are formidable concessions to the anti-property arguments which Becker dismisses in a mere 11 pages, laying most of the emphasis, incidentally, on the anarchist views of Proudhon rather than the critique of Marx.

One consequence of limiting 'possessive individualism' in this manner is a blurring of the distinction between property rights and other (non-proprietary) rights. Hence the idea of extending the applicability of the property concept to some of those non-proprietary rights is not quite as radical nor as surprising as it might at first appear.<sup>1</sup>

The New Property theorists nonetheless had a more radical goal than Becker. They wanted to redefine property in such a way as to go beyond the conventional identification of property with specifically

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1. Particularly when there is a general tendency to widen, indeed, inflate, the use of the concept of a right.

private property: an exclusive right to use, alienate or otherwise benefit from some thing. They argued that the scope or sphere of property is 'extended' if new types or categories of thing come to be recognised as subject to individual proprietorship. The growth of legal relationships between individuals and the state in advanced capitalism has created new forms of legal control over diverse resources which ought to be recognised as property. Some people, they suggest, have already begun to do so. Both Reich and MacPherson give specific examples of what they mean by 'new property', and both see licences as one such example: either as objects of property or as means by which rights of a proprietary character are transferred to individuals.

I shall now give some consideration to their ideas, briefly indicating what seem to me to be their principal shortcomings. It has been my argument so far that a New Property thesis might be based successfully on the theory of capitalist development outlined in the previous chapter, which assigns the state a limited but 'creative' role in this respect. The following writers, however, make different assumptions and, as a consequence, their arguments have serious weaknesses.

Easily the best of the New Property arguments is that of C.B. MacPherson who argues that the very idea of property as an exclusive individual right rests on the acceptance of a narrow

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paradigm of property.<sup>1</sup> Property is and must be an individual right but that right need not be a right to exclude others from the use or benefit of something. The equation of individual property with exclusive property is only a special case, and MacPherson advances a new paradigm which supplements the individual right to exclude others with an individual right not to be excluded by others from use or benefit from the social product: in other words, by an individual right to equal access to the means of labour and of life. The 'broad' paradigm proposed has two main features: firstly, it requires an equal right of access to the accumulated means of labour, whether social capital or natural resources (implying a right to work), and secondly, it is a right to an income from the social product, unrelated to work.

However, MacPherson's argument has a historical dimension which is its principal support. He recognises that the liberal conception of property as an unlimited exclusive right has definite social and historical roots. Conceptions of property ultimately derive from the real conditions of social and economic life, and the prevailing conception derives from the development of capitalist society. It is, he claims, 'an invention of the seventeenth and eighteenth centuries',<sup>2</sup> and appropriate to a fully autonomous capitalist market society. Yet, advanced capitalist societies are moving away from the idea of property as exclusion. This development is rooted in the growth of state expenditure and intervention which has partly abolished

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1. Property, op.cit., and 'Capitalism and the Changing Concept of Property' in Kamenka and Neale (eds.), Feudalism, Capitalism and Beyond, op.cit.

2. Democratic Theory, p.122.

market control, and has rendered the exclusive conception 'less necessary'.<sup>1</sup>

MacPherson's approach is, therefore, first to assume a general connection between ideas of property and their socio-economic context, then to connect the liberal conception with the specific property-ownership relations characteristic of an early stage of capitalist development when market forces were allowed to operate with relatively few restrictions, and finally to conclude that changes in market relations resulting from state intervention are now leading to, and require, a change in this liberal conception of property.

However, this argument is flawed on several counts. Firstly, the suggestion that the modern conception of property represents a 'narrowing down' of the pre-capitalist or feudal one is highly contestable. It is certainly true that in seventeenth century England, for example, the term 'property' had a wide range of meanings. Locke defines it in this way, as 'Lives, Liberties and Estates, which I call by the general Name, Property'.<sup>2</sup> Similarly, Hobbes observed that

Of all things held in propriety, those that are dearest to a man are his own life and limbs; and in the next degree (in most men) those that concern conjugall affection; and after them riches and means of living.<sup>3</sup>

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1. Property, p.10.

2. Second Treatise of Government, section 123. He also uses property in a more restricted sense to apply to material possessions.

3. Thomas Hobbes, Leviathan, pp.382-3.



Nonetheless, such broad definitions of property, and the existence of a conception of property as an individual right of access to the common property, maintainable against others, does not allow us to generalise about a 'feudal' conception. In small but important urban areas where market relations had developed, early versions of the modern 'narrow' paradigm could be found.<sup>1</sup> It was from these areas that the 'burghers' or middle class began the activities that were eventually to undermine feudal economic relations, and it was the generalisation of their market relations and their conception of property as an exclusive individual right to use, alienate and to benefit that became a characteristic feature of the emergence of capitalism. Pre-capitalist society is excessively 'feudalised' by MacPherson to reinforce his argument for a return to an up-dated version of the alleged pre-capitalist conception of property which included rights to access and to a revenue: in modern terms, as including and allowing for claims to employment, social insurance, community action, participation, and state largesse.

A second criticism derives from MacPherson's emphasis upon the market. He is certainly correct in viewing the universal market as the major institutional change distinguishing the capitalist economy from its predecessors. However, the exchange relations of capitalism are bound up with relations of production which are

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1. A good account of this is contained in R.Schlatter, Private Property. It is worth recalling that capitalist relations of production had been maturing for more than two centuries before the Industrial Revolution: see M.Dobb, Capitalism Yesterday and Today, p.20. However, forced labour was often used instead of wage-labour: for example, the use of convicts in mining.

also relations of domination. The contrast between the 'appearance' of equality and freedom in market relations on the one hand and the social domination in capitalist production was a theme developed by Marx in 'Capital'.<sup>1</sup> By basing part of his argument for conceptual change upon changes in market relations, MacPherson runs the risk of misinterpreting developments in a part of the economic structure which are neither fundamental nor free from distorting elements. The indisputable contemporary fact that the market no longer does the whole work of allocation could be, and has been, interpreted in ways which have quite different implications for the liberal conception of property. For example, Becker can accept this fact (and many others which show that contemporary capitalism differs radically from its 'laissez-faire' predecessor) and still argue that a modified liberal conception is possible, and worth having.

This leads on to a third weakness. His preoccupation with changes in market relations leads him to attribute considerable significance to the element of economic planning introduced by the state, although he is also aware of how large firms also introduce an element of planning into the market. This has such significance for him that he is led to distinguish 'mature capitalism' from an 'immature' predecessor. Yet, as I have shown in the previous chapter, a considerable degree of social control is compatible with, and even essential to, the further development of capitalism. The

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1. Capital I, esp. chapter 6.



persistence of the 'narrow' liberal conception of property might well be that it remains, in spite of the transition to 'quasi-market society', relevant to capitalist market and production relations.

Charles Reich is another theorist who, like MacPherson, sees property as becoming essentially a right to a revenue, and who also bases his argument for an extension of the application of the term 'property' upon changes in the role of the state.<sup>1</sup> He argues thus.

For an increasing number of individuals property has become a right conferred by or dependent on state largesse and state licence. This represents an unintended and incidental effect of the emergence of the state's new welfare and regulatory roles, and endangers one of the classical functions of property: the securing to an individual of an area of freedom from domination by society or the state. The state now has command of vast material and organisational resources, and has the ability to reward, to deprive and to frustrate prospective and actual recipients of those resources. For example, it has the ability to invalidate a driver's licence, to withdraw a professional licence or to deprive an individual of employment by the state. He notes that a precondition for the changing role of the state is a massive expansion of man's influence upon the material environment. States now have a means of social control in their ability to extend or withhold goods, services and other resources. Because the 'new

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1. Charles Reich, 'The New Property', op.cit.

property' is dependent on state fiat and executive and judicial interpretations of legislation, it does not secure but invades the area of individual freedom. Apart from the obvious comment that, in the view of many writers like Rousseau and Marx, property rights have never provided protection for such an area of individual freedom for the vast majority of people, there are several criticisms that can be levelled at Reich's argument.

The idea that state largesse tends to erode individual freedom as it expands is one which Reich himself has difficulties with. He examines a list of state functions and notes that some benefit private firms. He concludes that state power 'falls unequally on different components of the private sector',<sup>1</sup> and that largesse can be a form of assistance for private firms, especially in the award of leases for publicly owned resources. Largesse may thus create a partnership which aids rather than limits the private sector. The public sphere may, he admits, be used by private interests in their conflicts with other interests, and so this 'great system of power created by government largesse' can become a means to advance some particular interests. This represents a considerable weakness in Reich's argument: his initial assumption of an antagonism between state and private individuals is only supportable when it is subjected to several important qualifications.

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1. op.cit., p.764.



Indeed, Reich's conception of the state leaves much to be desired. He claims that 'the emergence of government as a major source of wealth' is a new development, and that these new forms of wealth are replacing private property. But where does this wealth come from? What are the causes of this new role for the state? Reich provides no answer to these questions, and his analysis lacks the kind of historical perspective which might make the origins of state largesse less mysterious. A broader historical perspective than the post-war period might have suggested that the state's expanded role could in part be located in the failure of the institution of private property to do some of the work of social and economic organisation necessary for 'economic growth' or capital accumulation. By concentrating solely on state functions and by taking as given the state's expanded role, Reich gains much plausibility for his view of the 'decline' of private property and his estimation of state power. However, the expanding role of the state during that period developed alongside an unprecedented expansion of the capitalist economies, which produced a large number of 'multinational' corporations whose capital resources exceeded the GNPs of many nation-states. Reich indirectly acknowledges this phenomenon in the qualifications he makes which I have mentioned in the foregoing paragraph. The absence of a broad theoretical framework in Reich's analysis has the effect of underestimating the many constraints upon state intervention.

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Much more than MacPherson's theory, Reich's is time-bound to the period of uninterrupted state intervention which followed the Second World War. This is the real basis for his exclusive focus upon the state as the source of 'new property'. The types of new property to which Reich refers display an emphasis upon the welfare roles of the modern state which recent events have shown to be unwarranted. The rights which have been granted through the welfare state are usually passive or recipient rights, which are held concurrently with a considerable degree of control by government officials and professionals. These rights do not have the same or even a similar degree of significance for social and economic organisation in a capitalist society as those rights in productive property discussed in section two of the previous chapter (that is, property rights). Since such rights have become no less important in the real world, it is surely unjustified to make conceptual changes which would have the effect of blurring distinctions between such very different types of right?

The same dependence upon rights created by the state's welfare roles occurs in Wolfgang Friedmann's argument for a redefinition of property.<sup>1</sup> He claims that property is confined less and less to the control of tangible things and is being 'extended to the whole field of legitimate economic interests and expectations'.<sup>2</sup>

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1. Wolfgang Friedmann, Law in a Changing Society.

2. *op.cit.*, p.117.



This is only a little less vague than his assertion that the right to use one's labour and skill should be considered a property right. Conveniently, Friedmann's radical redefinition does not presuppose any redistribution of the objects of property rights. His criticism of the inequality in property ownership is confined to a criticism of the unequal protection of property rights - although of course the courts have been quite consistent in what they do since they have not included his 'objects' in their category of property. However, Friedmann's redefinition of property might well obscure inequalities which really do persist. It may have the effect of making the law of property conform to popular aspirations about equality, but it would do so only by concealing the real situation, which remains one in which property is unequally distributed. If this is a contemporary 'social fact', albeit an unpleasant one, then surely we might ask that it not be concealed.

This redefinition of property has to be rejected for several reasons. Firstly, there has been no actual redistribution of property, and therefore an 'extension' of the current juridical conception to include certain relationships between legal subjects and legal objects, along the lines he indicates, would lead to a loss of clarity. Secondly, while the social and economic significance of legal ownership is beyond doubt, it is only specific types of property which have this important role. Legal rights

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arising from the activities of the 'welfare state' can only be considered rights of property at the risk of losing sight of the fundamental role of one particular type of property - property in the means of production. A more plausible explanation of the phenomenon of 'increasing protection' of rights which he identifies is that more people are now involved in legal relationships than before, though not necessarily proprietary ones. Finally, Friedmann, like Reich and even MacPherson, has too simple a view of the state's interventionist role, whether in respect to welfare functions or to economic ones. The state is seen (by implication here) as a neutral institution and little or no weight is given to those theories which see it as having a thoroughly partisan character. This of course makes it much easier to see it as a vehicle for the creation of new forms of property which co-exist and perhaps compete with specifically private property. In describing his own conception of property as 'more elastic' than the traditional one, Friedmann makes an assessment which is certainly appropriate.

A principal source of weakness for these redefinitions of property lies, then, in their almost indiscriminate search for new forms of property, so long as they involve some element of legal dependence upon the state. However, instead of looking at rights created by the state's welfare roles as examples of 'new property' rights, a much better case for the existence of a 'new property' could have been made with reference to the state's increasing economic functions, which all of the above writers identify but which do not receive the same attention as the welfare functions.

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Perhaps the reason for this emphasis upon welfare rights is to be found in the general (liberal) perspective of the above writers.<sup>1</sup> The ability of these writers to connect notions of 'property' and of 'individual rights' to the rights of real individuals, as opposed to corporations, is increased to the extent that they focus upon rights created by the expanded welfare functions of the modern state. To designate these rights as rights of property might seem, to some liberal writers at least, to represent a return to the 'basic model' of property-ownership in liberal thought: that is, the model of a single individual or family unit owning a tangible 'thing' like a plot of land. This is all the more reassuring at a time when the rights in productive property remain concentrated in a very few hands and when much control is exercised by corporations rather than the single individuals in the basic model.

Nonetheless, most liberal writers have rejected such an approach to conceptions of property, and therefore I shall not attempt to generalise from the above writers' arguments. My concern here is not with liberalism and the conceptions of property associated with it, but, more narrowly, with the question of the significance of new legal modes of holding property which involve the state to a considerable degree. This is a question they have asked, but not answered adequately.

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1. The inclusion of MacPherson here is justified since, in spite of his quasi-Marxist approach, he is concerned to 'retrieve' what he considers of value in the liberal-democratic tradition, and often seems to make assumptions about, for example, individual rights, which are shared by some variants of liberalism.

## 2. New Property - in practice

On the face of it, the system of petroleum licensing seemed to be an example of the transfer of rights which are de facto though not perhaps de iure rights of property. By focussing upon the socio-economic consequences for the holder of these rights, I showed that an analogy of licence rights with property rights was possible. Moreover, the resemblance of these rights to rights of property is greater, and has in my view a broader significance, when one considers the general trend toward tolerance of legislative restrictions upon the exercise of property rights in advanced capitalism, as well as the extra-juridical security provided by the close links between private firms (especially the large ones) and the state. The full extent of private dominance is masked by a legal form which appears to depart from that most closely associated with private power in capitalism: private property.

However, there are certain disadvantages in analysing any legal institution in terms of its socio-economic function, and I have made some attempts to avoid relying solely on that kind of approach here by examining the specific form of the licence, and by explaining how it assumed that form. To characterise this approach as 'functionalist' merely because it is concerned with inter alia the social and economic consequences of particular legal institutions seems to me to be misledding. It is widely known that Karl Renner

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conducted an intensive study of the 'social function' of legal institutions like private property, basing himself upon his particular conception of Marxian theory.<sup>1</sup> However, it is less widely known that Franz Neumann, a member of the Frankfurt School, who wrote much on the Rechtsstaat and its relationship to Fascism, also focussed upon the 'social function of legal institutions like property in his studies.<sup>2</sup> Unlike Renner, Neumann's approach was in the mainstream of modern Marxist thought and was associated with a view of capitalist development as a contradictory process which could not be understood in terms of 'evolution'. Indeed, a concern to discover the socio-economic consequences of specific institutions like private property seems to be an important component in Marxian social theory, and it is therefore not surprising that those Marxists who have examined legal institutions should have paid attention to it. If, as Anthony Giddens argues, this makes them (and Marx) guilty of a functionalist bias, then there may be something to be said in favour of functionalism!<sup>3</sup>

Nonetheless, it may be worthwhile to reconsider in some detail the formal characteristics of the petroleum licence which assumed significance in this study. To begin with, one of the most striking conclusions of the empirical study was that before

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1. Karl Renner, op.cit.

2. For example, in the various essays collected in The Democratic and the Authoritarian State.

3. His comments to this effect are set out in Central Problems of Social Theory.

licences could function as a vehicle for the transfer of property-rights, the licence form was modified to suit the intended function and acquired certain unusual and perhaps unique characteristics. As I explained in section 3 of chapter one, the character of the petroleum licence was altered by the Petroleum (Production) Act 1934 in such a way as to distinguish it from most other forms of licensing. It became more than just an 'administrative permission', and the contractual character which licences acquired as a result provided the licensee with a considerable degree of legal security for the rights transferred. While it is quite correct to assert that, until 1977 at least, licence rights allowed private firms the kind of effective control usually associated with rights of property and that most of the state regulation was facilitative, it does not follow that other forms of licensing, regulating different economic activities, have or might have this effect. We cannot generalise about licensing per se in contemporary capitalism from this particular case in spite of the fact that petroleum licensing, more than any other form of licensing in the UK, seems to be an example of one kind of property holding which the New Property theorists claimed was becoming increasingly significant.

Indeed, the self-description of this legal form as a 'licence' is perhaps a misnomer. In the United States the term 'lease' has much the same meaning and in the UK, the terminology of the petroleum production licence, permitting the licensee to get petroleum which

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once possessed is his, whatever its status before that, secures the same result as a mining lease: that is, it entitles its holder to exhaust rather than use the leased property. The House of Lords has described the mining lease as tantamount to a sale of minerals in place.<sup>1</sup> Despite the fact that the licence makes no explicit conveyance of the petroleum in situ, English law recognises, under the name of profit à prendre, a right to take the produce of another's land (for example, to fell and take away timber, or to catch fish) which is a property right in the sense that it can be invoked against any third parties that interfere with its exercise. It is this kind of right which, by reason of its exclusivity, and the conferment of a right to take from the soil, a petroleum production licence most closely resembles. In Scots law the comparable institution is the lease of mineral rights, which also conveys a real right to the resources of land not owned by the possessor of that right.<sup>2</sup>

Of crucial importance to the licensee is the exclusive character of his right to search and bore for, and get, petroleum under a specific licence area, which ensures that he may act directly to restrain any unlicensed drilling or other exploratory drilling in that area. Possessors of profits à prendre and analogous rights have, in the past, been held able to prevent unlawful invasions of their interest in many cases.<sup>3</sup>

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1. See their decision in Gowans v. Christie (1873) 11 M.(H.L.)1.
  2. See Rankine, The Law of Leases in Scotland (third edition, 1916), p.2.
  3. For example, Mason v. Clarke [1955] A.C. 778 (a dispute about rabbiting rights); and Stephens v. Snell [1939] 3 All E.R. 622 (invasion of exclusive fishery rights).

In the USA too, this particular economic activity has created problems for traditional legal forms of property, especially with regard to property rights in petroleum in situ. Some States like Texas have held that oil is like a hard mineral and is vested in the owner of the surface, who could deal with it as with other minerals by sale or licence; others like Oklahoma and Indiana have held that it is incapable of ownership in situ and can only be the subject of a personal right to explore; still others like Pennsylvania and California have held that ownership was not absolute until the oil was brought to the surface and reduced to possession, but pending this step, the landowner has a definable real right in the oil in the ground, similar to a profit à prendre or a lease.<sup>1</sup>

These particular characteristics of the licence distinguish it from the many other types of licence which are common in the UK: wireless licences, gun licences, dog licences, and so on. Such licences are regulatory in character, granting the holder exemption from legislative prohibitions, for reasons ranging from revenue-raising to the preservation of standards. By contrast, the Petroleum (Production) Act 1934, which was the basis of the subsequent legislation for offshore territory, ensured that petroleum production licences had the character of a concession by the Crown of some of its rights to a private party. This characteristic is shared by licences for the continental shelf although

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1. Manual, p.222; see also John M. Blair, The Control of Oil.



the rights possessed in that case and conceded by the Crown are not the same as those held on land. Not surprisingly then, the licences became contractual in form and displayed certain elements of a commercial transaction like the assignment by the Crown over a specific period of certain valuable rights, in return for annual payments, royalties on the produce of those rights, and, in some cases, premium payments also. This contractual element supplements the regulatory elements which are still involved in the licensing process, both in the rules governing the method of allocation and in the content of the licences themselves with their model clauses regulating working methods, safety, and so on, and reserving to the Minister considerable powers of discretion over the licensee's activity. This combination of contractual and regulatory techniques represented by petroleum production licensing is unusual and makes it *sui generis*.

Since licence rights have, for practical purposes, incidents more or less akin to leasehold property, subject (as such property commonly is) to restraints on assignment, it is not particularly surprising that they should have socio-economic consequences for the licensee similar to those which rights of property have for a lessee. The conclusion seems inescapable that petroleum production licences have changed most of their legal form better to fit their actual function.

However, as I have shown, the changes in legal form were not entirely successful in combining an element of regulation with the provision of conditions necessary for exploration and exploitation. The combination of contractual and regulatory elements presented a serious problem when the licence terms were amended in 1975. I

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have dwelled on this at some length in order to show how various procedural devices were introduced to resolve what I termed a 'crisis of legality', as well as to argue that the increased regulatory content of licences did not have the adverse impact upon licensees' interests that one might have expected. The network of legal and extra-legal techniques (consultations, 'talks', negotiations, and so on) was designed to minimise not only the uncertainty created by the Government's particular proposals, but also to assure the licensees (and others) that the general relationship between the state and private interests, in which state intervention plays a facilitative role, was not altered by the co-existence of regulatory elements with contractual ones in the licence. In attempting this the Labour Government was certainly successful, and the practical consequences of any tensions between regulatory and contractual elements in the licence were not particularly important in the longer term. Indeed, tensions were only visible at certain moments: for example, when the terms of existing licences were actually being revised, and in a more complex way, in the establishment of BNOC. Such moments had passed away by the late 1970s, giving the earlier period from 1974 to 1977 an 'exceptional' character. The unusual character of the events of this period is greater when it is recalled, firstly, that they were a response to the first world oil crisis and were carried out at a time when all national governments were hastily

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attempting to co-ordinate their energy policies; and secondly, that an increase in state intervention is the general rule once considerable reserves of oil are discovered: the British case is perhaps unusual only because the award of so many licences before this time rendered retrospective change necessary on a large scale.

Furthermore, the tensions between different elements in the licence was far from being a purely legal or formal matter. They were inseparable from particular economic interests. In particular, the Government's intention to use the state as a state and revise the terms of existing licences created dangers for British 'international capital'. The Government appeared to be treating licences as mere regulations which could be varied at Parliament's sovereign will, an action which might endanger the legal arrangements by which British companies' and banks' overseas interests were safeguarded, particularly in the United States. The structure of 'civil society' in Britain compelled an attitude of respect toward existing licence rights.

The co-existence of regulatory and contractual elements in the licence form has, however, a more general significance. The problems it presented when licence terms were to be amended represented in a particularly vivid way a basic antagonism which must follow from the state's self-presentation as sovereign power or licensing authority on the one hand, and as a quasi-private individual on the other. An elaboration of this idea has

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been given by Pashukanis, who argues that the close association of law with the phenomena of the market: equal individuals buying and selling commodities, including labour-power, of their own free will, and so on, gives legal relations a character antithetical to the relations of power and domination characteristic of the state. In a capitalist society, 'law' and 'state' exist uneasily as partners but also as opposites. Once the state becomes increasingly involved in market organisation the latent tension between the two also increases. There is much in the foregoing empirical study to support this view (at a general level at least), but since a pre-occupation with the form of the licence as opposed to its socio-economic consequences is only a secondary theme in this study I do not claim that this view is in some way 'confirmed' by it.<sup>1</sup>

The co-existence of contractual and regulatory elements in the licence also had a legitimating significance in this case. In particular, the association of property in oil with 'the nation' and the regulatory element in the licence helped conceal the extent to which North Sea oil has been, and continues to be, exploited by predominantly private interests. As I explained in chapter two, the idea of oil as 'national property' was exploited in

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1. Of course there is now a considerable literature on this theme of the contradictory character of state intervention. Many writers with different and opposing perspectives see this phenomenon as one which contains risks for the capitalist character of these societies. Jürgen Habermas, for example, sees a conflict resulting from the fact that the state is supposed to perform many economic and redistributive functions without violating the functional preconditions of a capitalist economy ('Legitimation Problems in the Modern State', in Communication and the Evolution of Society). In a similar vein, James O'Connor has argued that the attempt of the state to meet welfare demands while also trying to advance the capitalist economy generates a fiscal and general political crisis of the modern state (The Fiscal Crisis of the State).



political debate from 1963 onward. Its vagueness permitted its utilisation by Conservative Government to support a policy of maximising the involvement of British based private companies in North Sea developments, and by Labour Governments to support<sup>2</sup> similar policy but with the addition of some participation by state companies. However, from 1974 on, the notion acquired a much greater significance when it was associated with a considerable increase in the regulatory aspect of licensing. A considerable effort was made by the Government to mask the degree of continuity in North Sea oil developments, and especially the role of private companies and financial institutions, by pointing to the juridical changes being made as illustrative of sovereign power and social control through the state.<sup>1</sup> This was, as I have already pointed out, part of a broad response to a crisis of legitimation which manifested itself at the time in an outbreak of the sort of class conflict, which some had thought obsolescent in post-war capitalism.

These aspects of the licence form have been important in my examination of the various socio-economic consequences deriving from possession of a petroleum licence. A failure or an inability to distinguish between superficial and essential elements in the licensing process can quite easily lead to an overestimation of the degree of real (i.e. economic) change brought about by specific legal developments. The many legal qualifications placed

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1. The extent to which the Government clung to the idea of majority state participation in form at least is perhaps the best example of this.

upon the licensee's control over oil should not obscure the fact that the key right is not the right to possess oil in the ground, but to take the produced oil and to convert it into something else, whether it is money or a commodity like synthetic fibre. Further, the ability to obtain this right will be dependent upon the exclusive possession of the capital resources required to explore for and to exploit the resource. So long as the oil companies have possession of the massive resources required to develop oilfields in high-cost areas like the North Sea, they have the power to persuade states to give them that right and any associated rights. The starkness of this fact may, however, be concealed beneath the apparatus of legal regulation and participation which a state is obliged to introduce for purposes of securing legitimation or facilitating oil development or securing a share of the benefits for other private interests which operate in less profitable sectors of the economy. A growth of this 'superstructure' can provide evidence of a decline in the role of private oil companies and perhaps even partial erosion of their economic power. It has been my argument, however, that such an assessment of the empirical data produces wrong conclusions, and that my own view not only allows for a more complex interrelationship between social, economic, legal and political phenomena, but also helps explain the remarkable resilience of private power in this case. I do not

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claim that the view of law and state as highly influenced by the 'needs' of capital accumulation would find the same degree of support in a study of, for example, the sorts of citizens' rights which Charles Reich also considered important. Rather I have tried to show how, in one particular case, a legal institution can be so flexible that it can incorporate an increased quantity of state regulation, much of which is advantageous to the private parties concerned, and yet have similar, if not quite identical, socio-economic effects as before.

Actions taken by the British Government from 1974 to 1977 to extend the state's proprietary control solved a number of serious problems for the transnationally operating capital units involved.<sup>1</sup> This was not the result of some predetermined process but one in which initially critical and radical demands for social control through the state were transformed into ones not unacceptable to the beneficiaries of the status quo. Demands which, if given legislative form, would have resulted in radical alterations in property arrangements were not simply thwarted or ignored. Instead they were made to 'fit' certain dynamic forces pushing for change in the existing framework for North Sea oil development.

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1. For example, the existing arrangements had by 1974 ceased to be regarded as acceptable by a broad section of opinion in Britain (pp.132-4 above). The oil price rises and consequent windfall profits created a situation in which the oil companies could no longer be assured of public consent to their offshore operations and needed to act to restore their credibility. In addition, the bigger companies and the state had an interest in orderly offshore activity and hence in the resolution of a number of regulatory problems which had not been anticipated when the first regulatory framework had been drawn up 10 years earlier (see pp.178-85). In particular, a market had been developing in licence interests since 1972 over which the state had no control. The Conservative Government had responded by imposing a temporary prohibition on transfers of interests. Yet such 'assignments' were (and are) essential for smooth economic operations in the North Sea. New regulations were required to replace the old (and evidently inadequate) ones (see pp. 183-4)

At no point did I argue that these particular legislative acts and Government agreements were essential to the international private concerns. Rather I argued that some state action was essential in order to restore credibility to the licensees' operations in the eyes of a sceptical and hostile public at a time (1974) when both Government in Britain was extremely weak and future profits from the North Sea looked immense. In addition, the regulative, facilitative functions of the state<sup>1</sup> could not be carried on effectively once fields reached the development stage without extending the legal framework. Some form of Government action was essential: that it took the particular form it did was the result of a complex process in which the oil companies, the banks and others in sympathy with the interests of 'international capital' played a crucial role.

The theory of capitalist development outlined in chapter five is a considerable asset in explaining both the flexibility of this legal institution, and also the legitimating character of much of the law-making process itself.<sup>2</sup> Above all, it shows how a real basis can exist for perceptions of a partial abolition or 'transcendence' of private property and the articulation of redefinitions of property which are, at the present time, premature.

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1. Cf. pp.287-8.

2. I have discussed this in general on pp.287-90 above. The specific ways in which this legitimization function influenced the Government actions between 1974 and 1977 are set out on the following pages: (participation) pp.211-13, pp.223-37 (Harold Lever's remarks) pp.223-4 and also the paras. on pp.232-33, 250-52; (new regulations) pp.194-95, pp.319-20, pp.132-34, pp.167-68.



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NB. Although the interviews conducted in 1976 were an important background source, their informal character together with assurances to the interviewees about attribution, precluded direct quotation and compelled caution in use of this material. Consequently, I have avoided relying solely on remarks made in any one interview to substantiate a point in the text. Where I was unable to find corroboration in a published source for any material used, I compared the results of several interviews for agreement on the particular point before using this material.